

TO PROVIDE FOR THE ESTABLISHMENT OF A FEDERAL MORTGAGE BANK

HEARING

BEFORE A

SUBCOMMITTEE OF THE
COMMITTEE ON BANKING AND CURRENCY
UNITED STATES ^{Congress} SENATE

SEVENTY-FOURTH CONGRESS

SECOND SESSION

ON

S. 2914

A BILL TO PROVIDE FOR THE ESTABLISHMENT OF A CORPORATION,
KNOWN AS THE "FEDERAL MORTGAGE BANK", CREATING A PERMANENT
DISCOUNT AND PURCHASE SYSTEM FOR MORTGAGES ON URBAN REAL
ESTATE, DESIGNED BY COMPREHENSIVE YET CONSERVATIVE ACTION,
TO FILL A GAP IN THE NATIONAL FINANCIAL STRUCTURE TO THE END
OF STABILIZING MORTGAGE PRACTICE, EASING MORTGAGE CREDIT,
AND BY THE ESTABLISHMENT OF AN ADEQUATE AGENCY PREVENTING
PERIODIC FROZEN CONDITION IN FINANCIAL INSTITUTIONS.

JANUARY 18, 1936

Printed for the use of the Committee on Banking and Currency



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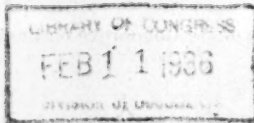
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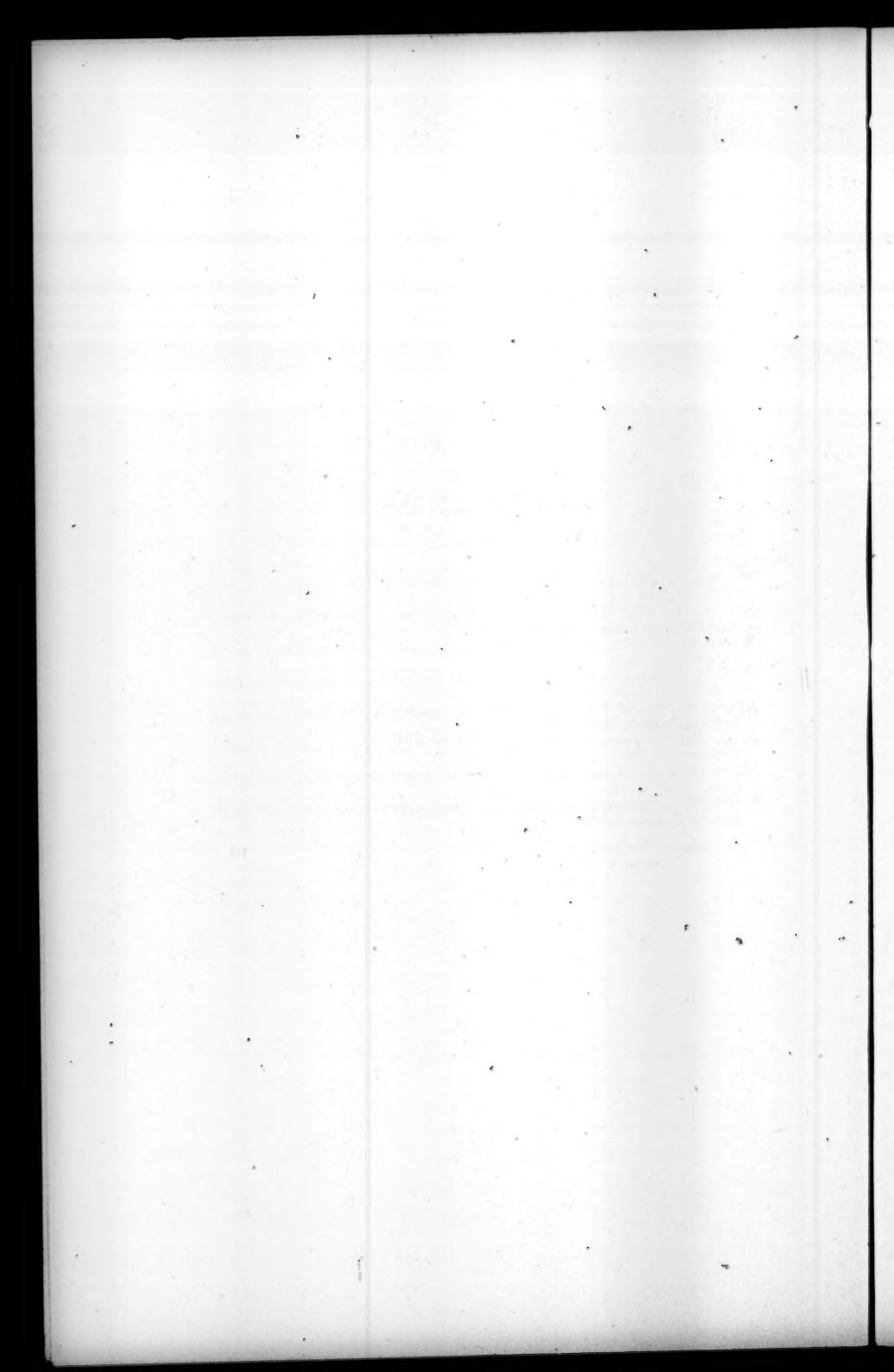


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TO PROVIDE FOR THE ESTABLISHMENT OF A FEDERAL MORTGAGE BANK

SATURDAY, JANUARY 18, 1936

UNITED STATES SENATE,
SUBCOMMITTEE OF THE
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The subcommittee met, pursuant to call, at 10:30 a. m., in room 301, Senate Office Building, Senator Duncan U. Fletcher presiding. Present: Senators Fletcher (chairman), Bulkley, Radcliffe, and Couzens.

Present also: Senator Wagner.

The CHAIRMAN. The subcommittee will come to order. Mr. Committee Reporter, this is a hearing before the subcommittee of the Senate Committee on Banking and Currency on S. 2914. The bill is as follows:

[S. 2914, 74th Cong., 1st sess.]

A BILL, To provide for the establishment of a corporation, known as the "Federal Mortgage Bank", creating a permanent discount and purchase system for mortgages on urban real estate, designed by comprehensive yet conservative action, to fill a gap in the national financial structure to the end of stabilizing mortgage practice, easing mortgage credit, and by the establishment of an adequate agency preventing periodic frozen condition in financial institutions

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be known as the "Federal Mortgage Bank Act."

SEC. 2. The President shall appoint as soon as practicable an organization committee of nine persons. The Secretary of the Treasury, the Governor of the Federal Reserve Board, the Chairman of the Board of the Reconstruction Finance Corporation, the Chairman of the Board of the Home Loan Bank, and the Housing Administrator shall be ex-officio members of said Committee. The remaining four members of said Committee shall be persons possessing a practical knowledge of real-estate and mortgage finance. A majority of the organization Committee shall constitute a quorum with authority to act.

The Committee is instructed to organize a Federal corporation, to be known as the "Federal Mortgage Bank", hereinafter called the "bank", to acquaint interested persons with the structure and functioning methods of the bank and to take pledges of subscription to its stock. The Committee shall serve for a period of six months from the date of its appointment; at the end of ninety days it shall report to the President the status of its activities.

The Committee is authorized to maintain an office; to employ legal counsel, expert aid, secretaries, and clerks, and to incur such other expenses as may be necessary in the express performance of its duties, but the total of its expenses shall not exceed \$75,000. The Reconstruction Finance Corporation is authorized to advance the amount of expense up to said sum, which said advancement shall be returned to the Reconstruction Finance Corporation by the bank if and when it commences operations.

SEC. 3. When the Committee has secured pledges of subscriptions to the capital stock of not less than \$10,000,000 from other than the Federal Government, the Committee shall notify pledgors to pay their subscriptions, and,

when stock has been paid for to the extent of \$10,000,000, the bank shall be declared ready for operation and, upon the filing of a certificate in due form with the Chairman of the Board of the Reconstruction Finance Corporation, the bank shall become a body corporate and shall have power—

First, to adopt and use a corporate seal;

Second, to have succession after the approval of this Act until dissolved by Congress or until forfeiture of its franchise for violation of law;

Third, to make contracts;

Fourth, to sue and be sued, complain and defend, in any court of law or equity;

Fifth, by its board of directors, to select, employ, and fix the compensation of such officers, employees, attorneys, or agents as shall be necessary for the performance of its duties without regard to the provisions of other laws applicable to the employment or compensation of officers, employees, attorneys, or agents of the United States, and to pay such proportion of the salaries and expenses of officers and employees of Federal or State agencies as the board of directors may determine to be equitable in proportion to their use by the bank in accordance with agreements with such agencies; to designate approved appraisers of real estate and servicers of mortgages at fees determined by it; and further to define the duties of its officers, employees, appraisers, and servicers, to require bonds for them, to fix the penalty thereof, and to dismiss at pleasure its officers and employees, appraisers, and servicers.

Sixth, to prescribe, by its board of directors, bylaws and regulations, not inconsistent with law, determining the manner in which its business shall be conducted and the privileges granted to it by law may be exercised and enjoyed.

Seventh, to exercise by its board of directors or duly authorized officers or agents all powers specifically granted in this Act and such incidental powers as shall be necessary to carry on the business of mortgage banking within the limitations prescribed by this Act.

Eighth, to create reserve funds and to declare and pay such dividends as may be earned by it and as, in the judgment of the board of directors, it is proper for the bank to pay.

The bank shall transact no business, except such as is incidental and necessarily preliminary to its organization, until it has been authorized by the chairman of the board of the Reconstruction Finance Corporation to commence business under the provisions of this Act.

Sec. 4. The bank shall be conducted under the supervision and control of a board of directors, consisting of nine members, holding office for three years (except as hereinafter provided for the first board) and selected as follows:

The President of the United States, with the approval of the Senate, shall appoint three members, two of whom shall be selected from among those who are heads or directors of Federal agencies dealing with the mortgage, and the third, a person possessing an especial knowledge of real-estate and mortgage finance who shall devote his entire time to the bank and be chairman of the board.

Six members shall be elected by the stockholders, not more than one of whom may reside at the time of his election in any particular Federal Reserve district as created by the Federal Reserve Board. No Senator or Representative in Congress shall be a member of the board, nor an officer or employee of the bank. Nominations for director may be made by any stockholder, but the nomination must be in writing and received by the bank at least thirty days prior to the date set for the election. The nominee to be eligible must have had practical experience in the business of real-estate and mortgage finance. With the nomination shall be furnished a statement of the nominee's experience in connection with real-estate and mortgage finance. Officers and directors of corporations or partners in firms which are stockholders shall be eligible to serve. Voting shall be by preferential ballot as now provided for the election of directors in classes A and B in Federal Reserve banks, one vote being recorded for each share of stock held by the stockholder. The chairman of the board of the bank, or, if he be unable to act, the vice chairman, is charged with the duty of seeing that a list and stated qualifications of the nominees for directors and a ballot is mailed each stockholder at least twenty days prior to the date fixed for the election. Voting may be by mail, but such votes to be valid must be formally signed and acknowledged by the stockholder.

Directors of the bank shall receive, in addition to compensation otherwise provided, a reasonable allowance for necessary expenses in attending meetings of the board.

The Committee shall handle the detail of the first election of the board. Appointments by the President for the first board shall be one director for one year, one for two years, and one for three years. Thereafter the annual appointment shall be for three years. Of the six elected directors, the two receiving the largest vote shall be declared elected for three years, the second two for two years, and the third two for one year. Thereafter the annual election shall be two directors for a three-year term. Vacancies that may occur shall be filled in the manner provided for the original selection of the directors, such new directors to hold office for the unexpired terms of their predecessors.

The board of directors shall elect a vice chairman and such other officers as it may deem necessary or desirable. The vice chairman shall be a director selected by the stockholders.

SEC. 5 The capital stock of the bank shall be divided into one million shares of \$1,000 each, nonassessable; five hundred thousand of said shares shall be common stock, and five hundred thousand shares shall be cumulative 4 per centum preferred stock, sharing with the common stock in dividends after the common has paid 6 per centum dividends.

The bank may sell stock only for cash and for no less than par.

No stockholder, except the United States, may hold stock in the bank in excess of 1 per centum of the bank's authorized capital. Any individual, partnership, corporation, the Government of the United States, or any State or subdivision thereof may be a stockholder.

National banks and other banks, members of the Federal Reserve System, as far as the legal effects of this Act may extend, are authorized to buy stock in the Federal Mortgage Bank to the extent of 1 per centum of the amount they have invested in mortgages, and may invest in the obligations of the bank, its notes, debentures, and other evidences of indebtedness; the obligations of the bank shall be lawful investments and may be accepted as security for all fiduciary, trust, and public funds, the investment or deposit of which shall be under the authority or control of the United States or any officer or officers thereof.

The Secretary of the Treasury, on behalf of the United States, shall subscribe to one hundred thousand shares, the authorized common stock of the bank, paying therefor, on call of the Committee or the directors, in such manner that it shall have paid in cash 10 per centum of the total cash capital made available to the bank. In order to enable the Secretary of the Treasury to make such payments, the Reconstruction Finance Corporation is authorized and directed to allocate and make available to the Secretary of the Treasury the amount of such sums, to be paid out of unappropriated balances. At the instruction of the President or of Congress, the Secretary of the Treasury shall pay the subscription on behalf of the United States in full or in such part as may be directed.

SEC. 6. The bank may lend on mortgages to, or buy mortgages from, persons, partnerships, funds, corporations, associations, and banking or other institutions complying with these two requirements: First, that they have been common-stock holders for at least six months prior to the proposed lending or purchase, and, second, that they are engaged in the business of using their own funds in the making of real-estate mortgages on urban property. The six months' period shall not apply to sellers or borrowers during the first eighteen months of the bank's existence.

SEC. 7. The bank may purchase or lend upon first mortgages, or other similar instruments of obligation defined in the Home Loan Bank Act, as amended, as eligible for lending, on improved urban property in such maximum and minimum amounts as the bank by regulation may determine, as follows:

(a) Any mortgage insured prior to July 1, 1937, under title II of the National Housing Act.

(b) Home mortgages (on single, and two-, three-, or four-family homes) not exceeding twenty years of life, amortized at the rate of not less than 2 per centum per annum, not exceeding 65 per centum of the fair worth of the property.

(c) Home mortgages unamortized not exceeding five years in life, and mortgages amortized at not less than 2 per centum per annum not exceeding fifteen years of life on multiple dwellings not exceeding 60 per centum of the fair worth of the property.

(d) All other classes of sound mortgages on improved property not exceeding 55 per centum of the fair worth of the property.

(e) Mortgages on property, where construction is to be started subsequent to the enactment of this Act and prior to January 1, 1937, at percentages to fair worth on above class (b), 75 per centum; on class (c), 70 per centum; and class (d), 60 per centum. The bank may commit that it will purchase or lend upon such mortgages prior to the commencement of construction, under regulations established by it requiring submission of plans, and other special acts.

SEC. 8. The bank shall require that these provisions, as they may apply, shall be met by the mortgage before it is declared eligible for lending or purchase:

(a) Mortgages must not exceed in the amount of unpaid principal thereof the maximum fixed by regulation nor be less than the minimum, and the maker thereof must not be in default for interest or taxes, or in any other of the terms of the mortgage.

(b) Before purchase or lending upon any mortgage, the bank shall require the member to furnish satisfactory evidence of the title to, and the fair worth of, the property given to secure the mortgage through sources approved by the bank.

(c) The mortgage practice of the stockholder must not have been found unsatisfactory.

(d) The bank is able to arrange for the servicing of mortgages transferred to it through approved agencies designated by it at reasonable fees.

SEC. 9. The bank may lend to responsible stockholders upon mortgages declared eligible up to 90 per centum of the unpaid principal due on said mortgages. The borrower shall execute his note, transfer the mortgage notes as collateral thereon, and shall endorse the mortgage and its note, which shall be deemed a waiver of demand, notice, and protest as to such borrowers' own endorsement exclusively. The loan shall be subject to such regulations as to maturity, interest rate, and other conditions as the bank may prescribe.

SEC. 10. The bank may purchase, from stockholders, mortgages declared eligible, paying therefor in cash 98 per centum of the amount due in principal thereon, plus accrued interest. The mortgage shall be purchased without the right of recourse against the seller thereof.

SEC. 11. The bank is authorized to issue notes, bonds, debentures, or other like evidences of indebtedness to obtain funds for the purpose of carrying out the intents of this Act, in the aggregate amount not to exceed twelve times its unimpaired capital and surplus. These notes, bonds, or debentures may be used for the purpose of exchange by the bank for mortgages agreed to be purchased; or may be sold by the bank as required and the proceeds of such sale used for the purchase of mortgages. Such obligations issued shall not exceed 90 per centum of the principal due on the mortgages owned by the bank plus the cash in hand, securities of the United States, notes of borrowers from the bank, and unpaid subscriptions to the capital stock, and shall be in such denominations at such interest rate and under such regulations as the board prescribes and shall mature within a period not to exceed twenty years from the date of issue. The regulations shall require that maturities of obligations of the bank and the principal payments to be made on mortgages shall be synchronized as closely as practical.

SEC. 12. The stock of the bank, and any and all notes, debentures, bonds, or other such obligations issued by the bank shall be exempt both as to principal and interest from all taxation (except surtaxes and estate, inheritance, and gift taxes) now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority. The bank, including its franchise, its capital, its reserves and surplus, its advances, and its income shall be exempt from all taxation now or hereafter imposed by the United States, by any Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority; except that any real property of the bank shall be subject to State, Territorial, county, municipal, or local taxation to the same extent according to its value as other real property is taxed. If and when the United States eliminates tax-free provisions on bonds issued or guaranteed by it, the same provisions as are made to apply to obligations of the United States shall apply to the stock, notes, bonds, debentures, and so forth, issued by the bank. The notes, debentures, and bonds issued by the bank, with unearned coupons attached, shall be accepted at par by the bank in payment of, or as a credit against, obligation of any debtor of the bank, or of any mortgagor whose mortgage it owns.

Neither the stock offering of the bank nor its subsequent offering of notes, debentures, bonds, or other such obligations need be subject to the approval of the Securities and Exchange Commission.

SEC. 13. When designated for that purpose by the Secretary of the Treasury the bank shall be a depository of public money, except receipts from customs, under such regulations as may be prescribed by said Secretary; and it may also be employed as a financial agent of the Government; and it shall perform all such reasonable duties as a depository of public money and financial agent of the Government as may be required of it. The bank may act as agent for any other instrumentality of the United States when designated for that purpose by such instrumentality.

SEC. 14. Subject to such rules and regulations as the directors shall prescribe, the bank shall have power to deal with, rent, renovate, modernize, or sell for cash or credit, or otherwise dispose of, with a view to assuring a maximum financial return to the bank, any property acquired by it as a result of foreclosure proceedings or otherwise.

SEC. 15. The bank shall semiannually carry to reserve account a sum not less than 25 per centum of its net earnings until said reserve account shall show a credit balance equal to 25 per centum of the outstanding capital stock of the bank. After said reserve is equal to 25 per centum of the outstanding capital stock, 10 per centum of the net earnings shall be added thereto semiannually. The funds in said reserve account shall be retained in cash or invested in obligations of the United States, except when the said reserve is equal to the outstanding capital stock any excess over that amount may be used to lend upon or purchase mortgages. Whenever said reserve shall have been impaired due to losses on defaulted mortgages, it shall be fully restored before any dividends are paid, excepting that such restoration need not be made as long as the reserve fund is an amount equal to the outstanding capital stock.

SEC. 16. The bank shall be examined in the conduct of its financial affairs in the same manner, at the same periods, and by the same agencies as are the national banks and shall bear the expense of such examinations. The bank shall give the findings thereof serious consideration through its board of directors and if defects in operating practice exist shall correct such defects as far as it may be able.

SEC. 17. The bank shall have its principal place of business in Washington, District of Columbia, but may establish branches in other cities as conditions indicate may be expedient, and may take such steps and make such deposits as are necessary to qualify it to do business in other States.

SEC. 18. The bank shall pay directors \$50 as a fee for each day required in traveling to and attending meetings. The compensation of the chairman of the board and of the members of the Executive Committee shall be at the rate of \$10,000 per annum each. If found desirable, it may create an executive committee of three of the directors, one of whom shall be the chairman of the board, who shall devote their entire time to the affairs of the bank. At least two of such executive committee shall be persons with a thorough knowledge of real-estate and mortgage finance.

SEC. 19. (a) Whoever makes any statement, knowing it to be false, or who ever willfully overvalues any security, for the purpose of influencing in any way the action of the bank or the board upon any application, advance, discount, purchase or repurchase agreement, or loan, under this Act or any extension thereof by renewal deferment, or action or otherwise, or the acceptance, release, or substitution of security therefor, shall be punished by a fine of not more than \$5,000 or by imprisonment for not more than two years, or both.

(b) Whoever (1) falsely makes, forges, or counterfeits any note, debenture, bond, or other obligation or coupon, in imitation of or purporting to be a note, debenture, bond, or other obligation, or coupon, issued by the bank, or (2) passes, utters, or publishes, or attempts to pass, utter, or publish, any false, forged, or counterfeited note, debenture, bond, or other obligation, or coupon, purporting to have been issued by the bank, knowing the same to be false, forged, or counterfeited; or (3) falsely alters any note, debenture, bond, or other obligation, or coupon, issued or purporting to have been issued by the bank; or (4) passes, utters, or publishes, or attempts to pass, utter, or publish, as true, any falsely altered or spurious note, debenture, bond, or other obligation, or coupon, issued or purporting to have been issued by the bank, knowing the same to be falsely altered or spurious, shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than five years, or both.

(c) Whoever, being connected in any capacity with the bank, (1) embezzles, abstracts, purloins, or willfully misapplies any money, funds, securities, or other things of value, whether belonging to it or pledged or otherwise intrusted

to it; or (2) with intent to defraud the bank or any other body, politic or corporate, or any individual, or to deceive any officer, auditor, or examiner of the bank, makes any false entry in any book, report, or statement of or to the board or the bank, or, without being duly authorized, draws any order, or issues, puts forth, or assigns any note, debenture, bond, or other obligation, or draft, mortgage, judgment, or decree thereof, shall be punished by a fine of not more than \$10,000 or by imprisonment for not more than five years, or both.

(d) The provisions of sections 112, 113, 114, 115, 116, and 117 of the Criminal Code of the United States (U. S. C., title 18, secs. 202 to 207, inclusive), insofar as applicable, are extended to apply to contracts or agreements of the bank under this Act, which, for the purposes hereof, shall be held to include advances, loans, discounts, and purchase and repurchase agreements; extensions and renewals thereof; and acceptances, releases, and substitutions of security therefor.

SEPARABILITY PROVISIONS

SEC. 20. If any provision of this Act, or the application thereof to any person or circumstance, is held invalid, the remainder of the Act, and the application of such provision to other persons or circumstances, shall not be affected thereby.

The CHAIRMAN. I have made an analysis of this bill, which I will not take the time to read because we want to hurry on with the hearing, but will ask the committee reporter to make it a part of the record at this point.

(The matter referred to follows:)

FEDERAL MORTGAGE BANK BILL S. 2914

Page 1: Section 1, title: "Federal Mortgage Bank Act." Section 2 provides that the President appoint an organization committee of nine persons, consisting of five ex-officio members:

1. Secretary of Treasury.
2. Governor, Federal Reserve Board.
3. Chairman, Reconstruction Finance Corporation.
4. Chairman, Board of Home Loan Bank.
5. Federal Housing Administrator.

Page 2, lines 6-7: Four appointed members consisting of "persons possessing a practical knowledge of real estate and mortgage finance." The above Committee shall serve for a period of 6 months. It shall organize the Corporation. It shall report to the President at the end of 90 days on its activities.

Page 3, lines 1-2: Its expenses limited to not more than \$75,000, said expenses to be advanced by the Reconstruction Finance Corporation and repaid "by the bank if and when it commences operations."

Page 5, line 8: Section 3, Corporation "shall be declared ready for operation" when—

Page 3, line 5: 1. \$10,000,000 is subscribed and paid up other than "from the Federal Government."

Page 3, lines 9-10: 2. "Upon the filing of a certificate in due form with the Chairman of the Board of the Reconstruction Finance Corporation."

The remainder of section 3 deals with general corporate powers.

Page 5: Section 4, the Board of Directors shall consist of nine members—

1. Selected as follows:

Page 5, lines 12-17: (a) Three to be appointed by the President and confirmed by the Senate, "two of whom shall be selected from among those who are heads or directors of Federal agencies dealing with the mortgage, and the third, a person possessing an especial knowledge of real estate and mortgage finance who shall devote his entire time to the bank and be chairman of the board."

(b) Six members shall be elected by the stockholders, not more than one of whom shall reside in any one Federal Reserve district.

Page 5, lines 21-23: (c) "No Senator or Representative in Congress shall be a member of the Board, nor an officer or employee of the bank."

2. Each director shall hold office for 3 years.
3. Salary of officers and directors is not fixed.

Page 6, lines 6-8: 4. Qualifications of officers and directors are confined to "officers and directors of corporations or partners in firms which are stockholders shall be eligible to serve."

Page 7: Section 5, capital stock—

1. Shall consist of 1,000,000 shares.

2. Par value, \$1,000.

3. Nonassessable (a) 500,000 common stock, (b) 500,000 cumulative 4-percent preferred, (c) after 6-percent dividends shall have been paid on the common, the preferred and common shall share equally in extra dividends.

Page 7, lines 21-22: 4. Stock may be sold "only for cash and for not less than par."

Page 7, lines 23-24: 5. "No stockholder, except the United States, may hold stock in the bank in excess of 1 per centum of the bank's authorized capital."

Page 8, lines 1-3: 6. "Any individual, partnership, corporation, the Government of the United States, or any State or subdivision thereof may be a stockholder" in the bank.

Page 8, lines 6-10: Any bank which is a member of the Federal Reserve System is authorized by this act "to buy stock in the Federal Mortgage Bank to the extent of 1 per centum of the amount they have invested in mortgages, and may invest in the obligations of the bank, its notes, debentures, and other evidences of indebtedness; * * *"

Page 8, lines 10-14: "The obligations of the bank shall be lawful investments and may be accepted as security for all fiduciary, trust, and public funds, the investment or deposit of which shall be under the authority or control of the United States or any officer or officers thereof."

Page 8, lines 15-17: 7. "The Secretary of the Treasury, on behalf of the United States, shall subscribe to 100,000 shares of the authorized common stock of the bank, * * *"

Page 8, lines 21-24; page 9, line 1: "The Reconstruction Finance Corporation is authorized and directed to allocate and make available to the Secretary of the Treasury the amount of such sums, to be paid out of unappropriated balances."

Page 9, lines 5-6: Section 6, "The bank may lend on mortgages to, or buy mortgages from, * * *"

Stockholders are subject to two requirements:

Page 9, lines 8-10: 1. "That they have been common-stock holders for at least six months prior to the proposed lending or purchase" and

Page 9, lines 10-14: 2. "That they are engaged in the business of using their own funds in the making of real-estate mortgages on urban property. The six months' period shall not apply to sellers or borrowers during the first eighteen months of the bank's existence."

Page 9, lines 15-20: Section 7, "The bank may purchase or lend upon first mortgages, or other similar instruments", the eligibility of which is established under the Home Loan Bank Act, as amended, and in such amounts as "the bank may by regulation determine", pursuant to the following limitations:

Page 9, lines 21-24: "(a) Any mortgage insured prior to July 1, 1937, under title II of the National Housing Act.

"(b) Home mortgages (on single, and two, three, or four-family homes) not exceeding twenty years of life, amortized at the rate of not less than 2 per centum per annum, not exceeding 65 per centum of the fair worth of the property.

Page 10, lines 1-19: "(c) Home mortgages unamortized not exceeding five years in life, and mortgages amortized at not less than 2 per centum per annum not exceeding fifteen years of life on multiple dwellings not exceeding 60 per centum of the fair worth of the property.

"(d) All other classes of sound mortgages on improved property not exceeding 55 per centum of the fair worth of the property.

"(e) Mortgages on property, where construction is to be started subsequent to the enactment of this act and prior to January 1, 1937, at percentages to fair worth on above class (b), 75 per centum; on class (c), 70 per centum; and class (d), 60 per centum. The bank may commit that it will purchase or lend upon such mortgages prior to the commencement of construction, under regulations established by it requiring submission of plans, and other special acts."

Page 10, line 20: Section 8, compulsory eligibility provisions with respect to mortgages are:

(a) The unpaid principle of the mortgage shall be within a maximum amount to be "fixed by regulation" of the board; all taxes and interest must have been fully paid up. Taxes and interest must be paid up and all other terms of the mortgage supplied.

(b) "Satisfactory evidence of the title to, and of the fair worth of, the property" securing said mortgage shall be given "through sources approved by the bank."

(c) "The mortgage practice of the stockholder must not have been found unsatisfactory."

(d) "The bank is able to arrange for the servicing of mortgages transferred to it through approved agencies designated by it at reasonable fees."

Page 11, line 13: Section 9, the bank may lend to responsible stockholders upon eligible mortgages "up to 90 per centum of the unpaid principal due on said mortgages. The borrower shall execute his note, transfer the mortgage notes as collateral thereon, and shall endorse the mortgage and its note, which shall be deemed a waiver of demand, notice, and protest as to such borrowers' own endorsement exclusively. The loan shall be subject to such regulations as to maturity, interest rate, and other conditions as the bank may prescribe."

Page 13, line 22: Section 10, eligible mortgages may be purchased by the bank, from stockholders, without recourse, at not to exceed "98 per centum of the amount due in principal thereon, plus accrued interest."

Page 12, line 3: Section 11, "the bank is authorized to issue notes, bonds, debentures, * * * et cetera. "In an aggregate amount not to exceed twelve times its unimpaired capital and surplus." Said obligations may be either sold to the public or exchanged for mortgages, "shall not exceed 90 per centum of the principal due on the mortgages owned by the bank plus the cash in hand, securities of the United States, notes of borrowers from the bank, and unpaid subscriptions to the capital stock." Denominations of bonds and interest rates on some are to be determined by regulations of the board; however, said bonds "shall mature within a period not to exceed twenty years from the date of issue."

Page 12, line 23: Section 12, obligations of the bank shall be tax exempt both as to principal and interest as long as the principal of tax exempt is applicable to other obligations. The issuance of securities by the bank is not "subject to the approval of the Securities and Exchange Commission."

Page 14, line 3: Section 13, the bank may be designated as a "depository" for public funds or employed as a financial agent of the Government; or any of its instrumentalities and "designated for that purpose by such instrumentality."

Page 14, line 15: Section 14, empowers the bank "to deal with, rent, renovate, modernize, or sell for cash or credit, or otherwise dispose of, with a view to assuring a maximum financial return to the bank, any property acquired by it as a result of foreclosure proceedings or otherwise."

Page 14, line 21: Section 15, the bank shall semiannually set aside as a reserve "25 percent of its net earnings until said reserve account shall show a credit balance equal to 25 percent of the outstanding capital stock of the bank", and thereafter "10 percent of the net earnings shall be added thereto semiannually." The reserves shall be kept in cash or invested in Government obligations. In the event the reserve has been impaired, dividends must be suspended until the reserves are restored.

Page 15: Section 16, national bank examiners are to make periodical examinations of the bank at the latter's expense. The board, however, is to determine its own standards.

Page 15, line 21: Section 17, the principal place of the bank shall be located in Washington, D. C., and empowered to establish such branches as it may determine. (Note: This section says that the bank shall establish, not that the board shall establish.)

Page 16: Section 18, the salary of the chairman of the board and of two other members of the executive committee shall be at the rate of \$10,000 per annum. All other directors shall receive \$50 per day for each day required in traveling to and from and attending meetings.

Page 16: Section 19, penalty clauses carry a maximum fine of not more than \$5,000 or by imprisonment for not more than 2 years, or both. And still a second penalty clause carrying "a fine of not more than \$10,000."

Page 17: Section 19 contains subsections each of which provides for fines of either \$5,000 or \$10,000 and imprisonment from either 2 to 10 years.

Page 18, line 14: Section 20, separability provisions.

The CHAIRMAN. I also sent out a questionnaire to about 400 people, and all replies have not as yet come in. However, I have an analysis of those replies we have received, which I wish made a part of the record at this point.

(The matter referred to follows:)

Answers to questionnaire on Federal Mortgage Bank Bill, S. 2914

	Yes	No	Doubtful, noncommittal, no answer
Industrial corporations.....	1	0	0
Real-estate companies and boards.....	31	4	0
Savings banks and trust companies.....	9	3	1
National banks.....	1	3	1
Mortgage broker, agents, and bankers.....	26	24	1
Miscellaneous.....	7	0	0
Attorneys.....	1	1	0
Life-insurance companies.....	2	1	1
mortgage guaranty companies.....	3	0	0
Savings and loan companies.....	1	0	0
State insurance commissioners.....	1	0	0
Total.....	85	36	4

The CHAIRMAN. I also wish to say that I have received, from time to time, a number of letters on this subject, and I will not burden the record with all of them; but, for the purpose of showing the rather typical views expressed, I wish made a part of the record at this point a letter received from Mr. L. A. McLean, president of Mortgage Bankers Association of America, also president of the Southern Trust Co., of Louisville, Ky., dated December 26, opposing the bill:

SOUTHERN TRUST CO.,
Louisville, Ky., December 26, 1935.

Senator DUNOAN U. FLETCHER,

United States Senate, Committee on Banking and Currency,
Washington, D. C.

DEAR SENATOR FLETCHER: Responding to your favor of the 20th, I have given a great deal of thought to the proposed Federal Mortgage Bank, and I am going to endeavor to give you my reaction to your questionnaire as fully as possible.

1. There is no necessity for a Government-chartered and supervised Central Mortgage Bank. There is a surplus of private funds available for sound mortgage investments in all parts of the United States, excepting only some remote areas where conditions are unfavorable, and where there will always be some difficulty in getting an ample supply of credit. The established mortgage-loan institutions, the building and loan associations, the mutual savings banks, the insurance companies, the fiduciary institutions, the trustee institutions, and the individual investors are seeking good mortgage loans everywhere at exceedingly low interest rates.

2. The existence of the proposed agency would not prevent the freezing of mortgage credit in times of stress. It would be impossible to distribute the debentures of the agency under conditions of stress.

3. The proposed Federal mortgage bank would not tend to reduce interest rates on urban mortgages unless general financial conditions were to dictate such a tendency.

4. I do not believe it would be possible with safety to have a Federal mortgage bank in addition to covering the home-mortgage field, to venture into the purchase of mortgage loans on large income properties or manufacturing properties.

5. Preference for Federal Housing Administration insured mortgages should absolutely not be given.

6. If it were necessary to have a Federal mortgage bank, it is my opinion that all reputable, experienced firms and corporations in the business of using their own funds for the creation of mortgage investments, should have the right to become stockholders.

7. Our institutions would not be interested in purchasing bonds of a Federal mortgage bank, especially if they were to bear interest rates from one-half to 1 percent above rates on Government bonds. I seriously doubt that many banks or financial institutions would be interested at all in purchasing this class of debentures at anything approaching the interest rates mentioned.

I believe that if the debentures or bonds of the Federal mortgage bank were exempted from taxation, it would be class legislation of a rather vicious character, and I am sure it would be unpopular. The exemption of the debentures of the Federal mortgage bank would place all the independent institutions in the same business at a very serious disadvantage. The taxpayers are becoming very firmly convinced that the tax-exemption feature on all bonds, municipal and Government, should be eliminated.

8. Certainly a billion-dollar mortgage corporation would have some influence on mortgage practices, and possibly to a lesser extent in having some of the real-estate laws amended.

9. Were there a Federal Mortgage Bank I would think that it should be permitted to make commitments under very rigid requirements to purchase mortgages on buildings to be erected. This is a very dangerous practice, especially on account of the lien laws in some of the States.

To sum up my important objections to the proposed bank, the purpose would be to set up a corporation with a capital of \$1,000,000,000, of which the Government would provide \$100,000,000. In order to be in position to do business with the corporation it will be necessary to own one share of stock costing \$1,000, and as the only incentive to purchase the stock would be to have the outlet for mortgage loans, it would be necessary to find 900,000 stockholders. To empower this corporation to issue tax-exempt securities would be class legislation, and contrary to the demands of taxpayers which is becoming more vehement that tax-exemption features be removed from all classes of securities. The President of the United States would be empowered to appoint the chairman of the board of directors, plus two other directors, each of whom would be connected with a mortgage enterprise of the Government, so it would eventually resolve itself into a Government-controlled Central Mortgage Bank, to which you will find great opposition.

No mortgage loan is any better than the servicing which that loan receives during its entire life. The proposed bill would permit stockholders to sell mortgages to the bank without recourse, and the bank would then have to evolve a very expensive system of servicing the mortgages, which would be weakened by the fact that those concerned with the servicing would have no direct obligations such as they would have morally had they been responsible for the actual making of the loans.

I have had a long experience in the mortgage-loan business, and I am convinced that instead of making it possible for the mortgage-loan business to function steadily throughout a depression, a depression would pull down the very foundation from under such a top-heavy corporation, that our Government would be compelled to step in to save the situation. I am convinced that such a corporation could not weather a depression similar to what we have passed through, without Government aid on some very large scale, and that is not to be desired.

My reaction to the tenor of the bill is—that it was designed to serve the purposes of the realtors of this country, who are in fact borrowers instead of lenders. They have advocated a central mortgage bank for some years as an aid to them in consummating real-estate sales. It would be very unsound.

I am glad to have had the opportunity to give you my personal views, and if I can be of further service to you, I will do my best.

Yours very truly,

L. A. McLEAN, *President.*

(Pen and ink notes.) We have many millions invested in urban mortgages in Kentucky, Indiana, and Tennessee.

And, on the other side, a letter from the American Radiator & Standard Sanitary Corporation, dated January 6, 1936:

AMERICAN RADIATOR & STANDARD SANITARY CORPORATION,
New York, January 6, 1936.

HON. DUNCAN U. FLETCHER,

United States Senate, Washington, D. C.

MY DEAR SENATOR FLETCHER: Answering your letter of the 20th ultimo, I beg to return herewith the questionnaire which you enclosed therewith.

Federal mortgage banks such as you have described I am sure would prove of great value in rectifying the existing mortgage situation. Short-term mortgages, with consequent high rates for renewals, bonuses, and commissions, have frequently brought the total rate for financing, after the current renewals, to 10 percent and upward, so that on the small house more than 30 percent of the total cost is sometimes paid for finance fees alone. This practice should be corrected. I am delighted to observe that a man of your distinguished reputation and understanding of these financial matters has undertaken to study these problems.

The removal of building, in the manner you have outlined in your questionnaire, from the speculative to the investment field, with long-term mortgages to be paid off in installments, will result in a demand for improved methods of construction and thereby assure the soundness of investment and financing, since under proper auspices no loans would be made unless specifications submitted with all applications therefor were carefully examined by competent and honest officials specially trained for such work. Such practice will inevitably create an incentive for improved methods in all the industries concerned with building, and construction will begin to play the part that informed people are increasingly coming to believe it should play in our economic and social destiny.

The Credit Foncier of France has conducted business on the basis you have outlined for more than 75 years, and has proven to be a sound and helpful instrumentality. Its debentures are among the most attractive of any in that country and, until the recent flurry in France, were in great demand at rates as low as 2½ percent. I do not know what their rates are presently, but a number of years ago our company, which operates a factory in France, put up an office building in Paris and borrowed the money from the Credit Foncier at the rate of 4 percent per annum, with annual amortization covering a period of 75 years, at the end of which time the entire principal was to be paid off. When the franc went down to almost nothing a number of years ago we invoked the privilege under the mortgage to anticipate the full payment thereof. I presume their rates are much higher than 4 percent now since the rate of the Bank de France has only recently been reduced from 6 to 5 percent.

The building industry when operating normally employs, directly or indirectly from forest and mine through transportation, manufacturing and workers in the building trades, an aggregate of over 4,000,000 men and is one of the largest, possibly the largest, in the country all things considered. Before a home is completed and occupied it touches almost every department of our national industrial and commercial life. When that industry sinks into a deep decline it carries with it a depression in all business. That has been the record of the 45 years during which I have been connected with this industry.

A curious thing is revealed by statistics, which show that 8 months minimum and 11 months maximum after a continuing decline in building activity is started a stock-market panic occurs, followed by the usual business depression with all the ills and embarrassments of unemployment attendant thereupon. It is, then, important and vital that the building industry should be surrounded with a financial system under some sort of Federal supervision which will prevent inordinate booms incident to cheap money loaned by persons who are not qualified to examine the character and dependability of construction for in due course it contributes its full quota to the creation of a general collapse. In, I might say, the controlling if not the most influential industry in the country, since the larger part of its activities are dependent upon the heretofore short-term mortgages. Practically every real-estate mortgage matured during the recent depression and placed a weight upon the banking situation which was responsible for quite the largest measure of frozen, if not worthless, loans that were found in the portfolios of many banks.

Faithfully yours,

J. M. WOOLEY.

Also a letter from Mr. Hugh L. Clary, vice president, Bank of America, San Francisco, Calif.

BANK OF AMERICA,
San Francisco, Calif., January 20, 1936.

HON. DUNCAN U. FLETCHER,

*Chairman, Committee on Banking and Currency,
United States Senate, Washington, D. C.*

DEAR SIR: I am returning the attached questionnaire which I have filled in. I believe that a mortgage bank of the type you propose would be helpful. However, I have answered your second question, as to whether or not the existence of such an agency would prevent the periodic freezing of the mortgage credit in times of stress, in the negative. As I read the act, the mortgage bank's money for purchasing and lending on mortgages will come primarily from the sale of debentures, and, inasmuch as these debentures are not guaranteed, I do not believe that they will sell freely in times of stress. This was clearly illustrated by the attitude toward Home Owners' Loan Corporation bonds prior to the time they were guaranteed. Nor is there any provision in the bill, as I read it, whereby a mortgage bank could rediscount its own assets with some agency which had the power to issue currency. For these two reasons it would appear to me that at a time when everybody was needing to turn their mortgages into cash there would be no practical way by which the mortgage bank could raise the cash which was needed; nor do I believe that the public would consider these debentures as equivalent to cash at such a time in the absence of a guaranty.

I am not suggesting that these changes be incorporated in the bill, and I believe a mortgage bank would be a helpful thing in spite of these defects.

Very truly yours,

HUGH L. CLARY, *Vice President.*

The CHAIRMAN. The first witness this morning will be Mr. Wendell P. Barker, chairman of the Mortgage Commission of the State of New York.

Mr. Barker?

Mr. BARKER. Yes; Mr. Chairman.

The CHAIRMAN. If you will come forward to the committee table and take a seat opposite the committee reporter.

Mr. BARKER. Thank you, Mr. Chairman.

The CHAIRMAN. You will have to hurry because the Senate meets at 12 o'clock noon today, and we will have to get along as fast as we can.

Mr. BARKER. All right.

The CHAIRMAN. Mr. Barker, please state your name, residence, and occupation.

STATEMENT OF WENDELL P. BARKER, CHAIRMAN OF THE MORTGAGE COMMISSION OF THE STATE OF NEW YORK, NEW YORK CITY; RESIDENCE ADDRESS: YONKERS, N. Y.

The CHAIRMAN. Mr. Barker, have you examined this bill? If you have, we will be glad to have your views about it, stated in your own way.

Mr. BARKER. Senator Fletcher, I have not given to the particular bill before you a critical examination. My thought in coming before you today was to state my views and the result of the study by the commission, of which I am chairman, with respect to the general subject of mortgage banking and the necessity for that type of institution.

Within the last week our commission has caused to be filed with the Governor of the State of New York and with the Legislature

of the State of New York a report containing our recommendations as to the proposed legislation. The principal recommendation which we are making is for the establishment of privately owned and publicly regulated State mortgage banks.

This report is rendered pursuant to the provisions of the mortgage commission law of the State of New York, which, in addition to vesting in the commission jurisdiction over some \$600,000,000 or some \$700,000,000 of certificated mortgages, and the problems of salvaging and rehabilitating those mortgages, also is the problem of recommending legislation which will prevent a recurrence, if possible, of the evils which we believe led to the debacle as respects mortgage guaranty companies.

I have with me a copy of that report which I will be very happy to submit to the subcommittee for what it is worth.

The CHAIRMAN. Will the subcommittee desire to have that spread on the record?

Senator COUZENS. I do not think that it all needs to be printed in the record.

Mr. BARKER. I have also prepared a statement of the views of my colleagues and myself with respect to the subject of mortgage banking which I think will fairly well summarize what is in the rather bulky report which I will be glad to leave with you.

The CHAIRMAN. I think we will receive and file the report, and we thank you for it, and will put in the record your statement regarding it. I think that ought to go into the record.

Senator COUZENS. Yes.

The CHAIRMAN. And the report will be filed with the subcommittee.

Mr. BARKER. May I proceed, Mr. Chairman?

The CHAIRMAN. Yes.

Mr. BARKER. The mortgage bank idea is—

The CHAIRMAN (interposing). May I ask first, Mr. Barker, how was this commission created?

Mr. BARKER. This commission was created in the early spring of 1935, and the commissioners were qualified on the 23d day of February 1935, and we immediately undertook our tasks.

Senator COUZENS. Was the commission created by an act of the legislature?

Mr. BARKER. It was created by chapter 19 of the laws of 1935 of the State of New York.

The CHAIRMAN. How many persons compose the commission?

Mr. BARKER. There are three commissioners, my associates being Mr. Louis S. Posner and Mr. Lawrence B. Cummings.

One of the earliest moves that we made in the commission was the creation of what we called the bureau of legal research, which consisted of 8 or 10 lawyers, to whom was delegated the task of making an intensive and exhaustive study and search into the whole subject of mortgage banking, particularly as it has prevailed and been practiced in about 22 countries of the world. The report which I am leaving with you contains some rather interesting exhibits with respect to mortgage banking in these 22 countries and forms the foundation of the recommendations which we have made.

Senator WAGNER. Might I interrupt you right there?

Mr. BARKER. Yes, sir.

Senator WAGNER. In view of your exhaustive research, the result of which is shown in this report, it might be useful to the members of this subcommittee, and the only way to preserve it, as it seems to me, is to have it in the record.

Senator COUZENS. Do you mean this whole volume?

Senator WAGNER. Yes.

The CHAIRMAN. The analysis here may cover that.

Senator COUZENS. Yes; the analysis will cover it, and as the Senator from New York knows, hardly anybody reads hearings after they are taken down.

Senator WAGNER. Well, it is quite an important matter.

Mr. BARKER. There is other matter in this report which, perhaps, would not be germane to the particular subject we are here discussing, so that when you cull it out and confine it to the subject of mortgage banking it will really not be very bulky.

Senator WAGNER. Are you going to review that?

Mr. BARKER. Yes, sir. I am going to review it in this statement.

Senator WAGNER. All right.

The CHAIRMAN. Very well, Mr. Barker, you may proceed.

Mr. BARKER. The mortgage-bank idea is, of course, not new in the history of mortgage financing, but the form in which it is recommended to the Legislature of the State of New York is much more than a mere copy of foreign prototypes. It is essentially an adaptation of these foreign institutions to our native American traditions and needs. No two countries are strictly alike in customs, in habit, or in temperament of the people, and no legislation which fails to take these differences into account can long be effective. The mortgage commission has therefore very carefully canvassed the situations abroad and has compared them minutely with local conditions, in order to be able to recommend the most favorable approach to the entire problem.

We think that the mortgage investments to be held by the public in the future must be given three fundamental characteristics: (a) Liquidity, so that the holder of a mortgage investment may at all times feel that he can convert his investment into cash without serious loss, as needs may require; (b) certainty of income, so that the investor may be left in a position to feel secure that so long as he holds on to his bond or debenture, he will receive a minimum periodic amount thereon; (c) confidence in the security of the principal, so that every holder of a security issued by a mortgage bank may feel that it is an obligation of the bank which is adequately supervised by government authority and adequately regulated by sound and prudent financial management.

To achieve these ends, we have suggested that the legislature authorize the creation of mortgage banks, under the direct supervision of the superintendent of banks, and subject to limitations which will advance each of the requirements of mortgage investments which we have listed above.

The simplest way of expounding the problem will be to go through the requirements of the mortgage bank as we have planned it seriatim, and to explain the reasons that have led us to include each of these requirements and why we think these limitations will inure to the public interest.

The public investments issued by the mortgage bank are to be general obligations of the bank and not shares or participations in individual mortgages or groups thereof. This is a fundamental requirement of future mortgage financing. Our experience has shown that the practice of selling shares or participations in individual mortgages or groups, or of selling bonds secured by an individual mortgage or group, is unfair, calculated to deceive the public, and fraught with great danger.

In times of calamity, individual mortgages suffer default. Many of them, however, weather the storm. The purchasers of mortgage investments generally rely upon the recommendations of the issuing house. They are not in a position to discriminate between good and bad mortgages. The result is that the investing public is treated to the remarkable realization that not all of the investments are in the same class; some are good, some are bad. The disorganization which results from this situation has led the guaranty company into liquidation or rehabilitation, and has caused the winding up of nearly all of the mortgage houses in the State. This will be entirely avoided under the plan proposed, where mortgage banks will issue debentures which are their own direct obligations and are not individually secured by any of the mortgages held by the bank, but are secured on the other hand by the total resources of the mortgage bank, of every kind and description.

Experience has shown that the average investor in so-called guaranteed mortgage certificates and, even indeed, in guaranteed whole mortgages, had little or no knowledge of the character or worth of the underlying real-estate security behind the guarantee. In fact, the investor relied upon the guarantee, and in so doing he relied upon the integrity and standing of the company. But when the crash came the investor found in some cases that he had invested in vacant lands or in a country club, whereas his neighbor, equally ignorant at the time of investment, found himself interested in a high-class income-producing property. There is no reason why there cannot be applied to real-estate financing, so far as the public is concerned, the same principles of "spread" and "average" which are fundamental in the insurance business.

One assured in the life-insurance business may die on the day following the writing of his policy and another assured may live 50 years, and yet the life-insurance company, by reason of the distribution of the profits and losses over and among all policyholders, is able to meet its contractual obligations. While definite figures are not available, there is little room for doubt that with a lower interest rate payable to investors and a pooling of the mortgages, notwithstanding the loose practices which prevailed with respect to appraisals, many of the mortgage companies would have been able to survive the recent economic collapse.

The next point—

The CHAIRMAN (interposing). What interest rate do you propose here?

Mr. BARKER. In the recommendations which we make we do not propose, nor could we propose by statute, any definite interest rate. Interest is like a commodity—it must be fluid, it must be fixed according to the economic conditions of the time. Bonds may be

issued at varying rates, 2 percent, 3 percent, 4 percent, or 4½ percent, whatever the particular conditions prevailing at the time may be. But however interest rates may differ, all debentures are debentures of the same class. They are merely issued in serials. I cover that a little more fully later on.

The CHAIRMAN. All right. You may proceed.

Mr. BARKER. Mortgages owned by the mortgage bank will be for long term and properly amortized. In the past, the custom has been for lending institutions to take mortgages for a 3- or 5-year period, requiring no amortization. As these mortgages were frequently renewed, it often happened that the mortgage indebtedness remained at the same level for 10 years or more, while the property continued to depreciate. Moreover, when defaults began to occur, practically all mortgages were in default on principal, and legislation enacting moratoria was made necessary. Investments secured by these mortgages were likewise in default. People who had planned to receive their principal within a given time were subjected to disappointment and frequently to serious inconvenience. The market for the sale of these investments collapsed due to the defaults, and bonds and certificates were sold at sacrifice prices.

Short-term-mortgage financing, experience shows, may prove equally disastrous to mortgagor and mortgagee. No mortgagee can afford to disregard the interests of the mortgagor and remain in a position where he must trust to the mortgagor somehow or other being able to refund or refinance himself at maturity date. The trouble has been with mortgage financing that neither mortgagor nor mortgagee seemed to realize that the transaction involved a debt which must be paid. In many cases of short-term mortgages the ink was hardly dry on the documents before the mortgagor was confronted with a problem of refinancing, all of which laid him open to renewal fees and expenses and rendered him averse to taking on any amortization burden. All this will be avoided by the mortgage bank, which will lend money on long-term mortgages properly amortized. Our proposal provides that mortgages shall be for periods of not less than 10 nor more than 20 years, and shall be amortized at a rate of not less than 2 percent per annum. These requirements will place in the vaults of the mortgage bank securities which will endure through long periods of time and will thus pass through various changes in economic conditions. At the same time, the constant payment of amortization will tend to enhance the value of the securities as time goes on, and they will furnish a sound basis for the issuance of debentures by the mortgage bank.

Appraisals are to be regulated and scientific: We have long been aware that many of the difficulties experienced in the past with regard to mortgage investments have been due to haphazard methods of appraisal. Agitation for the improvement of methods of appraisal has been going on in this State for a number of years. Appraisers themselves have organized to promote this end. The time has come when institutions which lend money on mortgage and sell their obligations to the public cannot be allowed to accept any appraisal that seems proper to them under the circumstances. Our plans call for rigid supervision of appraisals by the department of banks.

We wish to raise appraisers to a professional standing and to require each and every appraiser in the community to be licensed by the State, after having passed an examination with regard to his fitness and character. Mortgage banks will lend money only upon appraisals by licensed appraisers. Such appraisals will contain specific information required by statute, and will be subject to the disapproval of the superintendent of banks, so that, in the case of each loan made by a mortgage bank, the superintendent of banks will be in a position to pass upon the soundness of the appraisal. We believe that in appraising property more attention must be given to income, the present and convertible use of the property, trend of population and possible change in the character of neighborhood than to mere present principal value of the property.

This will result in scaling down the valuation by appraisers. While the proposed statutes require that no loan shall be made for more than 60 percent of the appraised value of any property, we think that, with this rigid supervision, the appraised value will be so low as to make the 60-percent requirement a very safe margin.

There must be personal responsibility for appraisals, and only individuals should be licensed, although corporations and firms, as in the case of insurance brokers and others, may act through designated, licensed individuals. With responsibility personal, with disciplinary action possible, even including revocation of license, there should be a tendency toward conservatism on the part of the appraiser. We are not foolish enough to believe that mere licensing in and of itself will make a good appraiser out of a poor appraiser.

I might interpolate here and say that we believe the recommendation to license appraisers is merely the first step toward raising the general standards of the profession. In the insurance business a battle was waged for years before we were able to obtain the licensing of brokers. After they were licensed the battle was carried on looking to a written examination of insurance brokers, and after we had accomplished that, then legislation was introduced requiring the serving of an apprenticeship in order for an applicant to receive an insurance broker's license.

I believe the American Institute of Appraisers, and other similar professional bodies, will join heartily in any and all suggestions to raise the tone and standard of appraisers. But all that we are doing at the present time is recommending governmental supervision through licensing.

The CHAIRMAN. All right, Mr. Barker.

Mr. BARKER. In addition to the benefits that will flow directly to the mortgage bank and to its debenture holders, great benefits will flow to the community generally from this supervision of appraisals. A wide equity will be left in each property which will be a fruitful source for junior financing. There is no reason why junior financing should not have a legitimate and proper sphere of activity in the community; and this method of regulating appraisals should limit first-mortgage loans to modest proportions, and thereby will provide a market which will not only enable the community to engage in junior financing, but will leave a satisfactory margin for equity holders to trade in from time to time and thus result in stimulating the real-estate activity throughout the State.

The mortgage bank will have adequate capital, surplus, and reserves. Our plans call for a minimum capital for each mortgage bank of \$3,000,000, and a minimum paid-in surplus equal to the capital, plus a reserve fund, to be accumulated from the net earnings of the bank, also equal to the capital. Thus a bank organized with a \$3,000,000 capital will ultimately have \$9,000,000 in capital, surplus, and reserves. Of this, the surplus and reserve fund, equal to \$6,000,000, is required to be liquid. This will form a substantial support for the outstanding debentures of the bank and will enable the bank to weather periodic storms that may occur. While in foreign countries we have found that there is no insistence upon the maintenance of liquid reserves and surplus funds, we believe that American systems and the psychology of the American investor require that such liquid reserves be established, if the confidence of the investing public is to be secured.

The fact that we suggest at the outset a surplus equal to the paid-in capital does not in the least reflect upon the character of the bank's operations. While the records in other countries show that the constant source of income from interest, amortization payments, and principal payments provides over the long term sufficient liquidity within the bank, we believe it to be wise, until the bank has been in existence long enough to provide for cash turnover and the consequent liquidity, to provide arbitrarily for a substantial surplus.

The extent to which the bank may issue debentures is narrowly limited by statute. We have found that, notably in the case of the Credit Foncier, the bank was authorized to sell its debentures to the extent of 50 times its capital. In other countries, however, narrower limitations obtain. We think that it is a good plan to limit the quantity of debentures that may be sold in relation to the capital and surplus of the bank. In the past no limit has been upon the certificates that may be guaranteed by a mortgage-guaranty company, or upon the bonds that may be sold by a mortgage-bond house.

While it is not entirely clear that such limitation is indispensable to the safety of the investments, or that it will add appreciably thereto, nevertheless we think that at the beginning, at least, this limitation ought to be put into the statute, and we have thus proposed that the mortgage bank shall not be permitted to sell debentures in excess of 20 times the capital and surplus of the institution.

Senator COUZENS. I notice that this bill, S. 2914, provides that such a bank shall not be permitted to sell debentures in excess of 12 times the capital and surplus of the institution.

Mr. BARKER. This is 20 times.

Senator COUZENS. Where do they get the 12 times inserted in the bill?

Mr. BARKER. Do you mean in the Fletcher bill?

Senator COUZENS. Yes.

Mr. BARKER. I do not know.

The CHAIRMAN. That is just preliminary and is subject to change.

Mr. BARKER. They vary. In my studies I find they vary from 8 times to 50 times, and we have arbitrarily selected 20 times as our judgment.

The CHAIRMAN. That is about right, I take it?

Mr. BARKER. And we have proposed that the mortgage bank shall not be permitted to sell debentures in excess of 20 times the capital and surplus of the institution. It may be that in later years it will be possible to extend this ratio, but at the present it seems a wise policy to include this limitation also.

The term of the bonds to be issued by the bank we think may be safely left to the judgment of its directors. In the case of Credit Foncier the bonds are usually for a term of 75 years, occasionally 50 years, and the shortest term of any of the bonds issued by that institution was 35 years. Should a mortgage bank issue its bonds for, say, 50 years, whereas its mortgages are for terms of 10 years, 15 years, and 20 years, it will produce the desired "spread", "average" and "turnover". Credit Foncier, established in 1852, in France, has weathered two major wars in one of which France was defeated and the other of which (the World War) it is claimed by many was more disastrous. In addition, Credit Foncier has survived an 80 percent deflation in the franc. No greater testimonial to the theory of long-term mortgage financing can be found.

The management and supervision of the bank: One of the most important items in the regulation of mortgage investments is the necessity of securing prudent management and adequate government supervision. We have included provisions in our proposed plan which are to that end, and provide both of these. In the first place, we have limited the board of directors to not more than nine people.

I might say at this point that we have received some criticism for that suggestion, it being argued that with a limited board of nine it might result in having a number of executive officials of a bank on the board, and consequently might end up in having so-called internal control. In fixing the number at nine it was purely arbitrary with us, and it is not a very material point in our recommendations.

A small group of that type will essentially feel a greater responsibility to the institution that it serves than the larger, unwieldy groups which manage other financial institutions. They will have a feeling of direct contact with the affairs of the bank which each director who assumes the office will at once realize and appreciate. Moreover, no one can be a director of a mortgage bank who does not first gain the approval of the Superintendent of Banks, and the Superintendent will therefore be in a position to make careful selection among financial people of the community, to that end that only those who have experience, ability and integrity will be permitted to serve these institutions. In addition, the bank is required to report—and I want to say that I consider this a very important item, gentlemen of the subcommittee—quarter-annually to the Superintendent of Banks with regard to all its transactions, giving particularly a statement of all defaults suffered by the bank during the period of the report, and all that has been done in connection with these defaults. The Superintendent is thus kept constantly in touch with the affairs of the bank; he is aware of what is going on within its walls; and he is enabled to take such steps as may seem wise to him from time to time to prevent, in advance of the event, the happening of any untoward contingency.

One of the greatest difficulties encountered today in the supervision of financial institutions by public authorities, such as the

Superintendent of Insurance or the Superintendent of Banks, has to do with man power adequately to check, supervise and examine these institutions.

It was very forcefully and fully brought out in the Moreland investigation, conducted a year or more ago at the direction of the Governor of the State of New York, that the best the superintendent of insurance could do was to get around every 2 or 3 years to make a real examination of insurance companies and mortgage guaranty companies. Our thought is that the subject of defaults being currently suffered by mortgage banks as respects payment of taxes and interest, is exceedingly important.

No truer barometer of the trend of events in a mortgage bank can be found than in the current record of defaults as respects the payment of principal, interest, taxes, et cetera. If, therefore, a quarterly, cumulative and running account of the occurrence and the treatment of defaults is required of the bank the supervising authorities will prevent many of the evils which have been laid at the doors of the mortgage guarantee companies in the past.

Payment of dividends: We think that those who invest in mortgage banks and who have the enterprise to carry on its affairs and to provide the service which it will inevitably have to give to the community, should be rewarded by fair and reasonable dividends; but we think that the business of the mortgage bank will be a profitable one, and that its stock will be widely sought by the financial fraternity in the State. At the same time, we have put provisions in our proposed legislation to prohibit the payment of dividends whenever the surplus funds of the bank or its reserves are in any way impaired, and we have imposed severe penalties upon the violation of this statute. We do not wish to see again a time when directors will declare dividends to their stockholders while their institution is suffering serious losses and the affairs of the investors are in a precarious condition.

As to the activities of the mortgage bank—

Senator COUZENS (interposing). Before you go into that, let me ask you this question: Is there any inhibition against discounting mortgages on vacant property?

Mr. BARKER. No.

Senator COUZENS. Shouldn't there be?

Mr. BARKER. We have given earnest thought to that. We think it is a question of degree and not of kind. We have conducted exhaustive investigations in our commission, with the result that many ideas have been exploded. I have had people suggest to me that a mortgage bank should absolutely prohibit consideration of vacant land, theaters, garages, hotels, or so-called specialties.

Senator COUZENS. Didn't you state a while ago in your testimony that there were found in the portfolios of many of these mortgage companies mortgages on vacant property?

Mr. BARKER. I did. But the difficulty with that was that the distraught investor found himself saddled with vacant land, without the benefit of income-producing property. In other words, experience has shown that where you get a wide cross-section of real estate, with intelligent and proper appraisals, there is nothing inherently dangerous. For instance, in putting into the general pot,

or the portfolio of the bank, all kinds of real estate, if it is intelligently appraised, there is nothing inherently dangerous.

Obviously—

Senator COUZENS (interposing). Why would you want a loan on vacant property? Wouldn't it be for speculative purposes?

Mr. BARKER. They do not loan on it, at least not necessarily. There might be a loan upon vacant property in a neighborhood which is growing fast, such as in some parts of the metropolitan area of New York. I can well conceive of situations such as my good friend, Mr. MacDougall, is connected with, developments in Jackson Heights, out in Queens, where the Queensboro Corporation went out into a vacant field, you might almost say, and developed that land, with 20 or 30 magnificent apartment houses, and with a surrounding golf course, and playgrounds, baseball fields, and all that sort of thing.

Now, that group of properties as an integrated whole is a magnificent thing, while that same thing if broken down and disintegrated would cause disaster. And when the Mortgage Commission came into jurisdiction and we were confronted with situations such as that, there was one group of certificate holders who had a mortgage on a baseball field, and there was another group of certificate holders that held a mortgage on a 15-story beautiful apartment house. The integrated whole would have stood up, but the disintegrated parts won't stand up. So that I do not believe we should jump too quickly into what may be error in just simply saying, out of hand, that vacant lands, theaters, garages, and specialties should be excluded.

I have given a good deal of thought to the mortality rate on different classes of property, and the results are sometimes surprising. We have always looked upon the private home, the home owner, as the outstanding risk; yet the records show from the standpoint of mortality—and by that I mean foreclosure—that it is very nearly at the top of the list, and you may be amazed perhaps to find out where theaters stand. I do not urge this as an argument for theaters or for vacant land, but I do say that before we arrive at any definite conclusions I think the subject has got to be very carefully analyzed.

I know of one company in New York, a mortgage-guaranty company, which turned its back definitely as a matter of policy upon all so-called specialty risks. But when the catastrophic collapse came, that company went down with the rest, was not able to weather the storm notwithstanding that policy.

Senator WAGNER. You began to say that we would be surprised if you were to tell us where theaters stand. Where do they stand?

Mr. BARKER. They stand very close to the top.

Senator COUZENS. What stands at the top?

Mr. BARKER. The better-class apartment houses.

Senator COUZENS. Just how do you determine the better class? What is the range between the worst class and the highest class?

Mr. BARKER. It is a little bit difficult to define that, except in the realty field there are the so-called classes of A, B, and C apartments, depending upon the rental value per room, the location, and the assessed valuation. For instance, there would be an obvious distinction between a Park Avenue apartment in New York and a multiple-dwelling tenement.

Senator WAGNER. In terms of rent per room, what would you say was the range as to the apartments you are speaking of?

Mr. BARKER. I would say the high-class apartment would rent for \$300 per room and up. In other words, where the rent for a five-room apartment would be \$1,500 a year, I would call that the better class of apartment.

Senators COUZENS. What are included in class C apartments?

Mr. BARKER. Tenements; cold-water flats.

Senator COUZENS. Haven't they fairly well wiped out those tenement places?

Mr. BARKER. That type of tenement is very disastrous in many respects, but there is now a wide movement sweeping over the country in favor of slum clearance, in favor of modernization and sanitation. We have today in the State of New York a law which was passed last year requiring the modernization and sanitation of the so-called cold-water tenements by means of fireproofing the halls and cellars and providing adequate toilets for each apartment. We are today confronted, in New York, with a very serious question of what to do with a great many of these so-called East Side tenements. Some of them would mean really a waste of money to recondition them and probably will be torn down. In fact, many of them are being torn down now with the aid of the Federal housing authorities, by W. P. A. workers.

Senator COUZENS. You said a while ago that apartment houses stood highest. What did you mean by that statement?

Mr. BARKER. I meant close to the top, Senator Couzens. I have not the actual conclusions before me, but I do know that they stand above private homes.

Senator COUZENS. You do not know which stands highest, do you?

Mr. BARKER. I do not know at the moment, Senator, but I could get it.

Senator COUZENS. Could you get for us a table showing the way relatively that these properties stand?

Mr. BARKER. Yes. I have a very good statistical and economic research bureau, which is giving very good thought to that subject, and later on I can give you our findings.

The CHAIRMAN. We would be glad to have you send that down to us.

Mr. BARKER. All right.

(The data requested, when furnished, will be printed in subsequent hearings.)

Senator COUZENS. Your remarks seem to be addressed to a State institution.

Mr. BARKER. Yes, sir.

Senator COUZENS. Just how do you propose to have that State institution tied up with a Federal mortgage bank?

Mr. BARKER. My feeling is that real-estate financing is essentially a local problem. I feel very deeply and very strongly on that subject. I believe it is the function of State mortgage banks rather than a Federal mortgage bank, although I do believe there is a great field for a Federal mortgage bank, or agency, or institution, with rediscounting facilities, so that there might be a tying in of Federal finance with local finance. But I would be disinclined to support the

idea of a Federal mortgage bank, say, operating from Washington, and perhaps finding it difficult to understand the conditions in Pleasantville, Westchester County, or some place in Olean, N. Y., and at the same time handling problems in Tulsa, Okla. In other words, I believe there is a field for a tie-up between the local institution and the Federal institution or agency, particularly for the rehypothecation or rediscounting of mortgages; and, above all, I do believe that a Federal mortgage bank should certainly be permitted to invest its funds in the bonds or debentures of local institutions, thus with the aid of Federal money coming to the assistance of local communities, it would enable our own institutions to take care of the financing of particular communities.

Senator RADCLIFFE. I notice a provision here that 25 percent of the net earnings should be set up in the reserve. Would it be feasible, under this plan, to attempt to put up a reserve before you attempt to estimate on your earnings? Your reserves are liabilities, as a rule.

Mr. BARKER. That is true. What we are recommending is that we start with a contributed surplus equal to the capital, and that then 25 percent of the net earnings of the company be set up in a reserve until that reserve equals the amount of the Capital. It is purely arbitrary.

Senator RADCLIFFE. Your reserve, then, is not based at all upon the amount of the risk?

Mr. BARKER. Oh, no. We limit it. We say the risk shall be 20 times the amount of the capital and surplus, so that an institution with \$3,000,000 capital and \$3,000,000 surplus could issue bonds to the extent of \$120,000,000.

Senator RADCLIFFE. Do you think it would be feasible to set up reserves on some percentage basis, similar to the way in which it is done with insurance?

Mr. BARKER. I do not, Senator, because one of the curses of the mortgage-guaranty business has been that there never was insurance, and I do not know of any way in which you can set up a reserve such as you indicate. You cannot have insurance without at least three absolute fundamental essentials: First, adequacy of premium or compensation for a risk assumed; second, an adequate reserve calculated from an actuarial standpoint; and, third, unless you have got a sufficient historical background of experience to establish a loan reserve.

Just let me amplify that a moment to show you how it breaks down. We know that in life insurance that when we pay a premium a certain part of that premium is for expense or loading or acquisition cost. We know that the balance of the premium which constitutes the so-called "legal reserve" is based upon some chart from an actuarial point of view, that if invested at a certain rate of interest, according to the American experience table of mortality, for the period of time that the assured is expected to live, will produce the face of the policy. That is an actuarial reserve.

In fire insurance we know from long experience, roughly speaking, that 50 cents of every premium dollar constituting the unearned premium reserve will be sufficient to take care of loss in return premiums in the business. So it goes right down the line.

But when you get to the mortgage guaranty business or the mortgage business there is not any way of calculating premiums or setting up reserve, and you have got either a feast or a famine. Experience has shown us in the mortgage guaranty business that it was profitable beyond dreams. In good times there were no losses. When you get an economic collapse, they are all losses. In case of fire insurance, if this building burns, the one across the street does not necessarily burn. In life insurance if I die, you do not necessarily die. But at a time of an economic collapse such as we have gone through in connection with real-estate values, if this plot of land goes down in value, that plot and that plot go down, and they all go down.

That is the reason why, in my judgment, you cannot tie the mortgage guaranty business up to the so-called "insurance theory of reserves". The only way you can solve it, in my opinion, is by the so-called "long-term mortgage financing", basing it, as I said a few moments ago, on spread and average.

Senator RADCLIFFE. If you do not follow the example of insurance companies, of setting up reserves as soon as the risk is assumed—and that is a liability of the company, and the capital and surplus cannot be determined until that reserve is set up—if you do not do that, do you not run into this rather anomalous situation? Suppose there are two mortgage companies. One is making a profit and the other one is not, and yet they are doing the same kind of business in a general sense. The company that is making a profit sets up 25 percent as reserve. The company that is not making any profit does not set up any.

Mr. BARKER. That is right.

Senator RADCLIFFE. Is not that rather inconsistent?

Mr. BARKER. The reserve is purely arbitrary, to provide liquidity or to prevent excessive dividends being paid in the absence of a reserve. My own feeling is, frankly, Senator, and our investigations as to foreign companies show, that once you get this thing turning over and with your interest payments coming in and your amortization payments and your principal payments, you have within the bank itself quite sufficient liquidity. Times get a little tight and you stop making loans.

I was amazed when I found in studying the set-up of the Crédit Foncier and in studying the set-up of the mortgage bank in Argentina and in Chile, that they considered there was no necessity for reserve. Perhaps if I had more courage I might not recommend a reserve. What I have done is to recommend the setting up, as I say, of a pure arbitrary surplus equal to capital and then having in mind the tendency of the American investor putting a little brake upon the payment until they have set up this purely arbitrary reserve, which serves only the purpose of adding to those so-called liquid funds which must be kept in non-real-estate securities.

Senator RADCLIFFE. Suppose reserve were set up equal to the capital, and that reserve is diminished—

Mr. BARKER. Then the reserve must be made up before any dividends can be declared.

Senator RADCLIFFE. The company can still operate?

Mr. BARKER. Oh, yes.

Senator RADCLIFFE. As long as there is any capital?

Mr. BARKER. As long as it has any capital; yes—unless the superintendent of insurance wants to stop them.

Senator RADCLIFFE. The existence of a reserve and the existence of a surplus would not be essential?

Mr. BARKER. Just for liquidity, pure arbitrary liquidity. Frankly, that is as I see it and that has been the history of the other institutions.

Senator WAGNER. What does the French institution do with reference to the bonds? Does it provide a sinking fund for their amortization?

Mr. BARKER. No. The bonds are, as we suggest here, redeemable, callable at will, so that they are always able to take care of a low money market. For instance, if they have got a series of bonds out at $4\frac{1}{2}$ percent and they are in a 3-percent money market, they have the right to redeem or recall those bonds and reissue and refund, just as the United States Government or any government does in its refunding operations, taking advantage of the market rate in interest.

Senator WAGNER. The Government has a sinking fund to eventually amortize its bonds, has it not?

Mr. BARKER. Yes.

Senator WAGNER. The French system does not provide for that?

Mr. BARKER. No.

Senator RADCLIFFE. The provision in regard to amortization suggested is 2 percent?

Mr. BARKER. Not less than 2 percent.

Senator RADCLIFFE. That is only the rate of normal depreciation?

Mr. BARKER. Yes.

Senator RADCLIFFE. So you are really not amortizing it?

Mr. BARKER. But at the same time if you have a conservative appraisal to start with and you do not want to make it prohibitive, if you are making a 20-year loan, as it has been suggested, so amortized as to pay the loan off at the end of the term, you get a prohibitive situation. In other words, you cannot very well have a 5 percent amortization and at the same time pay interest. It would probably result in crippling real-estate financing.

Senator RADCLIFFE. How much does a building and loan association pay off on the principal, on an average? Is it at least that, or probably more?

Mr. BARKER. I should think so.

Senator RADCLIFFE. Why should this percentage be so much less than ordinarily paid in a building and loan association?

Mr. BARKER. We feel we do not want to draw it too fine for mortgage financing. Just assuming for the sake of the argument that 2 percent represents normal depreciation, if you have got your cushion to start with of 40 percent due to a conservative appraisal, and your amortization is coming in all the time equal to the depreciation, we feel that the matter is safe.

Senator RADCLIFFE. Has not the experience of building and loan associations shown that the rate of amortization is not such an excessive burden and, further, that that rate is probably essential for the protection of the property?

Mr. BARKER. The building and loan association does business with home owners and people of that type. I question very much

whether on a large office building or a large apartment house in any urban center they can stand the strain of 4 or 5 percent amortization. I do not believe it would be possible.

Senator COUZENS. May I ask whether you contemplate that this mortgage bank shall be in such form as the Federal Reserve bank?

Mr. BAKER. Somewhat in that form; yes.

Senator COUZENS. Do you believe that this bank should interfere with private enterprise or compete with private enterprise?

Mr. BAKER. It is a private institution, Senator.

Senator COUZENS. But it is Government-regulated and Government-financed, as I understand?

Mr. BAKER. Not the bank that we are proposing.

Senator COUZENS. But the one in the bill?

Mr. BAKER. Yes.

Senator COUZENS. This bill is being discussed, not something else.

Mr. BAKER. Senator, I find on that subject that I have rather definite views. Ever since I have been chairman of the mortgage commission I have taken a very definite stand against any State agency or governmental agency competing with or contending with private enterprise. I would rather have strong governmental regulations than competition.

Senator COUZENS. I am interested in the bill and not what the State of New York may do. On page 9, section 6, it is provided that the bank may lend on mortgages to, or buy mortgages from, persons, partnerships, funds, corporations, associations, and banking or other institutions. If they may go into the field of making mortgages or buying mortgages from individuals or persons, partnerships, and corporations, is not that highly competitive?

Mr. BAKER. I should say it is; yes.

Senator COUZENS. I thought there was a campaign on to take the Government out of business.

Mr. BAKER. That is my view. I have thought very strongly, in the particular job that I am in, that I would rather see the Federal institution aid local institutions and be available for rediscount, rather than to have the Federal institution making direct private loans. I want to say, however, in expressing that opinion, that it is my own view and not necessarily committing my associates on the commission.

Senator RADCLIFFE. Do you think there would be enough facilities among State companies to rediscount each other's obligations?

Mr. BAKER. Perhaps not at the beginning, but I think it would soon come.

Senator RADCLIFFE. Without calling upon the Government?

Mr. BAKER. Yes. It might be necessary at the beginning, but as a long-term policy I would be opposed to it. I think there is a real need now for Government assistance.

May I just conclude this, and then I shall be through?

The CHAIRMAN. The question is whether there is a need for this kind of an organization, whether there is not a private field for private business and just have the Government supplement it.

Mr. BAKER. I think it can supplement it and be a powerful factor, sir.

Senator WAGNER. In reference to getting the Government out of business, I am as sympathetic to that point of view as anybody, but

it seems to be a slow process, perhaps. There was called to my attention the other day a proposal to construct a very large number of apartments, and an application was made by the corporation that intended to construct the buildings for a loan. I think it was a loan of \$2,000,000. The loan was to be insured so that there probably was no risk to the insurance company at all. At first it appeared to be an attractive proposition. Then it was discovered by those making the investigations that in surrounding territory the company held some mortgages and they were afraid if they made this loan, these new apartments being more attractive, with more modern improvements, it might affect the value of their mortgages, and, therefore, they declined to make the loan. There is a case of progress being impeded for a rather selfish reason, it seems to me.

Mr. BARKER. That is true.

Senator WAGNER. What can we do about a situation like that?

Mr. BARKER. I feel as a result of the collapse of the mortgage guaranty companies that we have practically frozen the public out of the real-estate investment field and that it is going now, and has been for the last 2 or 3 years, practically solely into the hands of the large financial institutions, like the insurance companies. That is wrong. In other words, we have either got to have mortgage companies or Federal banks, somebody that can step in here. I have had several cases in my own experience where they have declined. Insurance companies have declined to make loans because of the adverse effect upon something else.

Senator WAGNER. It prevents further construction.

Mr. BARKER. That is true.

Senator WAGNER. What are we going to do about that?

Mr. BARKER. We have got to either get the money through a mortgage bank of this character or through a Federal guaranty bank or F. H. A., or something of that sort. We have simply got to do it.

Senator WAGNER. F. H. A. is ready to insure this mortgage. Is there any other place to go but to a Government agency?

Mr. BARKER. Much as I deprecate it, one of the great problems I think we have in your State and mine, Senator, particularly in the metropolitan area, is the unwise new construction which is really not necessary. I think that is one of the greatest curses today—new construction.

Senator BULKLEY. What is your test as to whether new construction is wise or unwise?

Mr. BARKER. As to the number of vacancies and the availability of residential quarters and the advisability of modernization. I think one of the most attractive possibilities in New York today is rehabilitation and modernization of existing buildings.

Senator BULKLEY. Have you worked out any formula to figure out how you can apply the figures on vacancies to the problem of new construction?

Mr. BARKER. I have a chart on that. I do not have it with me. We are making an examination along those lines. I think our Commission, dependent upon certain decisions coming down from the Court of Appeals which we hope will be favorable, will probably have a great deal to do along the lines of modernization and rehabilitation.

The CHAIRMAN. That is pretty well covered by the F. H. A., is it not?

Mr. BARKER. Yes, sir.

Senator WAGNER. The experience up in my own neighborhood is that in modernizing some of these houses that did not happen to go to pieces altogether, houses of the very old type, while under former conditions they could not rent them at all, the moment they modernized them they were able to rent them. The poor fellow who owns a house has not the means to modernize it and does not seem, in spite of the efforts that are made, to be able to get the banks to advance money for modernization.

Mr. BARKER. It is very difficult to do.

Senator WAGNER. There is another stalemate, apparently. Yet I think it would help the section I speak of.

Mr. BARKER. Very much so. Of course, Senator, our great problem up there now is this, that we have plenty of real estate, plenty of mortgages, and plenty of money. The difficulty is in getting them to join hands and get this money flowing into the real-estate mortgage market. I think one of the great problems confronting our Commission, and other agencies like it, is the refunding and refinancing of these old top-heavy mortgages. I am working on some plans now which I think will go a great distance to accomplish that. For instance, to give you an illustration, I may have a \$100,000 mortgage on a piece of property that is appraised at \$100,000, and foreclosed. Obviously, the mortgage is top-heavy. If I can go to a life-insurance company and say, "On a present-day appraisal will you let us have a 60-percent loan on a 10- or 15-year mortgage?" and they say, "Yes." I take that \$60,000 and distribute it among the certificate holders, leaving them with a junior noninterest-bearing certificate or participation for the remaining \$40,000.

That will go a long way, in my opinion, towards liquefying the situation, getting new money to come in to the real estate field. There are literally hundreds of millions of dollars crying to get in, but everybody is afraid.

Last night I had a meeting up in New York with some very prominent real estate and banking interests, discussing this mortgage bank, and they seemed to feel that some method like this may be the spark that will start this refunding and refinancing.

Senator WAGNER. It is reported that many of these lending institutions that made unwise loans say that the loan they made is not the value of the building now, but in order to hold on and try, if possible, by gradual recovery to bring it back to where they thought it was originally, they are not lending money, because they do not want any construction to go on at all which may in some way affect their houses.

Mr. BARKER. I feel that is true.

Senator WAGNER. But that is a serious situation.

Mr. BARKER. It is serious.

Senator WAGNER. If it is going to have an effect upon our efforts at slum clearance I do not think you disagree that something should be done in order to proceed with slum clearance?

Mr. BARKER. Oh, no. We must do that. There is no doubt about it.

The CHAIRMAN. The suggestion you made about surplus and reserves—a system of that kind would tend toward stabilizing the whole situation, would it not?

Mr. BARKER. Yes, Mr. Chairman. I feel that in the illustration that I gave, if you had \$3,000,000 capital, \$3,000,000 surplus, and \$3,000,000 reserve, and that capital is invested in mortgages, it would start you on your way. If you keep \$6,000,000 in high-grade non-real-estate securities, then as against your \$120,000,000, assuming you reach that limit, you would have \$6,000,000 of liquidity, and that added to the normal liquidity from the income would be sound and safe financing, and I have had the advice of many bankers on that.

Senator RADCLIFFE. If it were once put up it would have to stay there?

Mr. BARKER. Yes; it would have to stay there. And the superintendent of banks is given the right at any time, of course, to step in and stop them from making any further loans, or stop them from paying dividends. That reserve is sort of a hybrid; it is a liability, as you say, Senator, but it cannot be used for dividends. It is just an arbitrary thing that is put in there for liquidity.

Senator RADCLIFFE. And once put there it would have to stay, even though failure to take it out would mean impairment of capital and the company would be called upon for new capital?

Mr. BARKER. That is right.

Senator RADCLIFFE. It would stay there how long?

Mr. BARKER. Indefinitely.

The CHAIRMAN. Do you think it is wise to use the term "bank"? It is not a bank; it does not receive any deposits.

Mr. BARKER. It is somewhat of a misnomer, Mr. Chairman, calling it a bank.

The CHAIRMAN. Would it not be better to call it a corporation or institution?

Senator WAGNER. I suppose you are afraid to call it a mortgage company?

Mr. BARKER. I was going to say, Senator, that there are certain names that are sort of not in good standing now.

There are one or two other observations that I would like to make, and then I think I will be through with this. The debentures issued by the mortgage bank while issued in series from time to time will all be of the same general nature as respects the security behind each series. That is to say, they will all be of one general class. Interest rates on the various series will vary according to the condition of the money market and it will be permissive for the bank, if its board so decides, to write into the debentures the privilege of permitting debenture holders to share in profits. The mortgage bank will be able to register and sell its debentures on the leading exchanges of the country. This should provide a ready market for the bonds, enabling the debenture holders to feel certain that they may at any time convert their holdings into cash. Debentures of this character have for many years been recognized and favored in Argentina where such debentures are traded in on the leading exchanges to a greater extent than perhaps any other security.

The bank will be permitted to redeem and to refund and will thus be able to take advantage of fluctuations in interest rates and a cheap

money market. By the use of amortization payments to buy in its own debentures on the public market, the bank will be able to prevent severe oscillations in price on exchanges. As a matter of fact, our investigations reveal that fluctuations in price on foreign exchanges of the securities of foreign mortgage banks have been very slight, even in the years of depression.

Mortgage banks, when organized, should be given a free and open field so that their business may prosper and the mortgage business of the state may be directed through these channels and others precluded from entering that field. In other words, we feel that we have got to be very careful not to interfere with legitimate corporate financing. You cannot stop a railroad from issuing its bonds, even though back of the bonds there may be a mortgage on a great deal of real estate. Nor can you prevent a corporation, which owns an office building, from issuing its corporate bonds to the public, even though back of those bonds there may be substantially nothing but real estate.

The distinction that we draw in defining a mortgage bank is that it is an institution which is organized primarily for the purpose of lending money on mortgages and selling its debentures to the public. Our investigations are still continuing, Senator, and I will be very glad, if there is anything that I can give you out of our economic and research bureau or statistical department, if you will indicate any character of information that you think would be helpful, to furnish such information as you desire. I will not promise to give it to you, but I will go the limit to get it for you.

The CHAIRMAN. We are much obliged.

Senator WAGNER. What is the attitude of the present lending institutions to the proposed mortgage bank?

Mr. BARKER. So far it has been very, very favorable—so much so that I am frightened. I wonder where the opposition is. One of the leading executives of the savings banks association during the last week has strongly endorsed it. We have discussed it with the various leaders of real-estate boards, such as the New York Real Estate Board. They seem to be very favorably disposed toward it; and I understand that the life-insurance executives are giving it favorable consideration.

Senator WAGNER. Would it be in competition with such institutions?

Mr. BARKER. To a certain extent. Of course, the savings banks and insurance companies will continue to make direct loans, too. I think they will loan large and small sums of money directly on mortgages on specific pieces of property. My thought is that we have got to find some way, if you are going to have real real-estate financing, to get Mr. John Public into it safely.

Senator WAGNER. Do you think you are going to sell them your certificates?

Mr. BARKER. We will sell them debentures. In the investigation we made we took some testimony. One man advanced the theory that you should not allow these bonds to be issued in denominations of less than \$2,500 or \$3,000. When I asked why he said, "Well, Mrs. Riley, with her \$500, should not be permitted to go into the real-estate business. She should keep her money in a savings bank."

Of course that sounds very well, but the difficulty as I see it, is that either the thing is sound or it is not sound; and why we should not permit Mrs. Riley to put her \$500 in a properly regulated real-estate investment, but allow her to go down to Wall Street and lose her money in anything she likes, I have not yet been able to answer. I see no more logic or reason in saying that you shall not invest \$100 in a real-estate bond than to say that you shall not invest \$100 in stock or bonds or any security that is on the exchange.

Senator RADCLIFFE. Do you think the insurance companies would be willing to buy these debentures rather than make corresponding loans?

Mr. BARKER. My thought is that they will do both, Senator, and to a large extent will buy the bonds of a mortgage bank. We are also proposing an amendment to the laws which expressly permit savings banks and life-insurance companies to buy these bonds.

Senator RADCLIFFE. Would not insurance companies be inclined to insist, as in the past, on the direct loan and direct contact?

Mr. BARKER. They, I think, will continue to make many of these large direct loans, but they have great difficulty today in finding a real outlet for all the money that they have to invest, and my judgment is that if they can get a cross-section of real estate through the bonds they will do so.

The CHAIRMAN. Do you know what interest savings banks pay?

Mr. BARKER. Anywhere from 3 to $3\frac{1}{2}$ and 4 percent.

The CHAIRMAN. Do they pay that much?

Mr. BARKER. Yes, sir.

The CHAIRMAN. That is about as much as these debentures would bear, is it not?

Mr. BARKER. Yes. I do not want to see these debentures particularly high. I should say 4 or $4\frac{1}{2}$ percent would be about the limit. If you are going to have them sound and attractive for the investor I do not think you can offer very high interest rates.

One of the curses of the past has been high interest rates required of mortgagors. Since all the mortgages are in the pot, so to speak, there will be nothing to prevent them in times of stress from reducing the interest rate by one-half of 1 percent or 1 percent, if need be, to the mortgagor. That is what the life-insurance companies did.

Senator RADCLIFFE. What difference do you think there ought to be as between what a mortgage pays and what these debentures pay?

Mr. BARKER. I confess it is just my opinion not yet followed through that there should be a differential of, say, $1\frac{1}{2}$ percent between the amount that the mortgage pays and the interest which the bond pays; and my reason for that is that I am told that the expenses of the bank should absorb roughly 1 percent, leaving roughly one-half of 1 percent.

The CHAIRMAN. The Federal Land Bank has a margin of one-half of 1 percent to cover the expense of administration.

Mr. BARKER. Yes, sir.

Senator RADCLIFFE. If that could be done, why should not one-half of 1 percent be put up as reserve without waiting for the question of the profits to be determined?

Mr. BARKER. I am open-minded on that. It has been suggested.

Senator WAGNER. That is pretty high, is it not?

Mr. BARKER. I should say it is plenty high. I think one and a half would be the absolute maximum of differential. We are having some investigations made, but it will not run more than one and a half.

The CHAIRMAN. Mr. Walter Rose, president of the National Association of Real Estate Boards, Orlando, Fla.

Mr. ROSE. Mr. Chairman, in view of the limited time, I am going to ask that Mr. MacDougall, chairman of our finance committee, and Mr. Walter Schmidt, immediate past president, present our arguments.

STATEMENT OF EDWARD A. MacDOUGALL, CHAIRMAN, FINANCE COMMITTEE, NATIONAL ASSOCIATION OF REAL ESTATE BOARDS, NEW YORK CITY

The CHAIRMAN. Mr. MacDougall, please state your name, place of residence, and occupation.

Mr. MACDOUGALL. Edward A. MacDougall; New York City; real estate.

The CHAIRMAN. Mr. MacDougall, you are familiar with this bill, are you not?

Mr. MACDOUGALL. Yes, Senator. I have some knowledge of the bill.

The CHAIRMAN. We will be glad to have you discuss it.

Mr. MACDOUGALL. With your permission, Senator, I should like to submit first for the record a resolution passed by the National Association of Real Estate Boards at its convention at Atlantic City, at which there were a thousand delegates represented. I will not undertake to read that resolution, or the one from the State of Florida, but they are characteristic of the resolutions that have been passed by real-estate boards throughout the United States, and I should like to leave with your office these records for your examination and reference.

[NOTE.—Resolution passed on October 25, at National Association of Real Estate Boards' twenty-eighth annual convention at Atlantic City, to Federal Mortgage Bank.]

NATIONAL ASSOCIATION OF REAL ESTATE BOARDS,
November 23, 1935.

Mr. E. A. MACDOUGALL,
Jackson Heights, New York City.

DEAR Mr. MACDOUGALL: Enclosed herewith is a copy of the resolution passed at our Atlantic City convention with reference to the Federal mortgage bank, as requested in your wire.

Following is an excerpt from the minutes of the directors' meeting which has to do with amendments to the Fletcher bill:

"It was moved by Mr. Harry A. Taylor, seconded and unanimously carried, that the committee on real estate finance be authorized to make such amendments as may be necessary in negotiations upon the passage of the Fletcher bill."

I presume that this is what you have reference to in your wire.

Sincerely yours,

HERR NELSON, *Secretary*.

RESOLUTION PASSED OCTOBER 25 AT NATIONAL ASSOCIATION OF REAL ESTATE BOARDS'
TWENTY-EIGHTH ANNUAL CONVENTION AT ATLANTIC CITY

Whereas the Federal Government has established various great instrumentalities concerned with mortgage finance; and

Whereas these agencies cover but a portion of the field and do not assure marketability of the mortgage; and

Whereas mortgage lending should be kept in private hands with such safeguards thrown about it as will make investors and institutions secure; and

Whereas the security resulting from the establishment of a Reserve system for long-term mortgage credit providing marketability would induce the lowering of interest rates: Now, therefore, be it

Resolved, That we urge the Federal Government immediately to provide a major agency upon some plan as that outlined in the Fletcher bill (S. 2914), and establish this agency as the focal point for synchronizing the work of various Federal corporations and administrations dealing with the mortgage to the end of inducing standardization of practice and providing marketability for the mortgage.

The CHAIRMAN. Very well. We will put those resolutions in the record.

Mr. MACDOUGALL. Our committee has sent to our membership, bankers, and mortgage investors throughout the United States, several hundred letters inquiring as to whether or not if this Federal Mortgage Bank were incorporated as provided for in S. 2914, they would invest in the stock of a Federal Mortgage Bank.

The second question was, "Will you cooperate in urging the passage of this bill?"

I have some 50 letters representing very responsible institutions on that subject. I should like to leave those also in the record for your consideration.

The CHAIRMAN. Very well.

Mr. MACDOUGALL. As you can see from our directors' resolution, we are quite prepared to recognize that bill which you introduced at the last session may have to be amended in some respects to satisfactorily meet the requirements or suggestions that we have developed in the course of the interval which has elapsed since the bill was introduced. Those recommendations we will submit to your committee at a later time.

The emergency feature of the Federal Mortgage Bank has been emphasized far too much, in our opinion, as against another far more important function of the bank. I refer to the transfer of funds from where they may be available to where they may be needed for mortgage purposes. That is one of the greatest functions, if not the greatest function, that this bank will exercise. It will have a tendency to equalize interest rates on mortgages throughout the country, as the Federal Reserve banks have done in connection with short-term financing. We cannot emphasize too greatly this function of the bank. The benefits which it would confer to the South and the West, where interest rates are proverbially higher than they are in the eastern section of the country, need no emphasis. The value to the investors in the east, in putting their money in first-mortgage securities in the West and South, is equally important.

We believe that a Federal mortgage bank should cooperate closely with the Federal Housing Administration, since that is a permanent agency set up by the Government, which has done already a great deal of good in encouraging loans and in creating new standards for neighborhoods and housing developments, upon which any sound mortgage structure must be based. The form which such a central mortgage-discount bank should take, in our opinion, has

been set forth in the bill introduced by Senator Fletcher at the last session of Congress. The bank may issue notes or bonds against mortgages held up to 12 times its capital and surplus. We believe that this type of privately conducted but publicly supervised agency is the best method of getting Government out of the private mortgage field.

We doubt if there is any other way in which this can be achieved.

We believe that the Federal mortgage bank should be free to deal in all types of urban mortgages. We believe that some form of sound mortgage bonds is desirable, as a safe investment for the savings of the public. We believe that mortgage bonds should be issued by a central agency so that standards will be uniform and liquidity assured.

We believe that a Federal mortgage-discount bank is necessary to the ultimate success of the State mortgage banks, which Mr. Barker, chairman of the Mortgage Commission of the State of New York, has so clearly defined to you and the committee this morning.

We are convinced that the mortgage associations, which are provided for in title III of the National Housing Act, are too limited. We ask that your committee, in its deliberations, take a broad view of this matter, and we hope that you will find it possible to recommend the passage of this bill by Congress, which will create a comprehensive Federal mortgage bank for urban mortgages.

Thank you, sir.

The CHAIRMAN. You will hand us later the proposals with regard to amendments?

Mr. MACDOUGALL. Yes, sir. We will do that; and, bearing directly on the bill, I would ask you to invite our former president, Mr. Walter Schmidt, to address you on those questions.

The CHAIRMAN. We will do that. When can you have those proposed amendments?

Mr. MACDOUGALL. In the course of a few weeks, or probably 30 days, we can submit something.

The CHAIRMAN. Very well. We would like to have it for the record.

NOTE.—At the time this portion of the hearing, part 1 on S. 2914, went to press, the above-referred-to amendments to be submitted by Mr. MacDougall and his association had not been received. They will be incorporated in subsequent hearings, reference to which will be made in the index or table of contents thereto.

The CHAIRMAN. The next witness will be Mr. Walter S. Schmidt.

STATEMENT OF WALTER S. SCHMIDT, CINCINNATI, OHIO, FORMER PRESIDENT, NATIONAL ASSOCIATION OF REAL ESTATE BOARDS

The CHAIRMAN. Please state your name, Mr. Schmidt, your place of residence, and your occupation.

Mr. SCHMIDT. My name is Walter S. Schmidt; my address, Fifth and Main, Cincinnati, Ohio. I am engaged in various businesses, including real estate, engineering, and so forth.

The CHAIRMAN. Mr. Schmidt, you have examined the bill, have you?

Mr. SCHMIDT. I have read the bill very carefully, Senator.

The CHAIRMAN. We would like to have your views about it.

Mr. SCHMIDT. My general views are these:

First, that it is an absolute function, and, further than that, an obligation of government, by directive action, to protect its credit structure.

The real-estate-mortgage credit structure has not been protected in the past. The short-term credit structure has its reserve system in the Federal Reserve banks, whereas the long-term, which is of much greater amount than short-term credit, has not only had no reserve system, but practically no directive action, whether that direction was in the practice followed in the operation of such an agency, or in such economic direction as would make for the stability of a mortgage system.

It is therefore our measured judgment that government must establish a comprehensive agency covering not only the housing of the Nation, but, as well, the other types of mortgage investment.

We feel that the mortgage structure is one unit whole, and that you cannot have collapse in one portion of that mortgage structure without pushing down the remaining portions of it. We therefore feel that Government has an obligation to cover that entire long-term-credit field by a measure or a group of measures that will provide marketability for the mortgage and a reserve system for the whole structure.

The sociological problems involved in housing and the farm have naturally first engaged the attention of Government in these recent years, but we feel, having studied the situation from every angle for many, many years, that one of the weaknesses of our situation has been that partial coverage of the field and the attempt to take it piecemeal.

It is our judgment that there must be a synchronization and a pulling together of the various agencies that are concerned with the mortgage, and that therefore the reserve system must cover urban mortgages of every type, in addition to the housing mortgage and the farm mortgage.

This bill, as I read it, does not do what Senator Couzens suggested in his statement, namely, permit the investment of a central mortgage bank directly in mortgages. As I read the bill, it definitely provides that the bank can buy mortgages only from originating sources. For that reason it is a supplementary agency to existing lending institutions and not an actor in the first instance.

The bill does provide that the Federal Government shall subscribe to a portion of the capital stock, and, in that respect, many might say that it was an entry of Government into business.

However, I invite your attention to the fact that subscription is limited to 10 percent of the stock of the bank. Inasmuch as Government properly should have some interest in this agency in order that it may secure the right of supervision and some control, it is my judgment that that is a very wise and necessary provision.

The CHAIRMAN. Is there any plan whereby that stock may eventually go out of the Government, or is the Government to keep that stock?

Mr. SCHMIDT. There is absolutely no reason why the Government could not, at any moment, sell that stock, so far as I read the bill.

The CHAIRMAN. What participation does it require on the part of the Government in the management of the bank or institution?

Mr. SCHMIDT. It requires that the President appoint three of nine directors, the remaining six to be elected by the stockholders, and that the bank shall be examined just as are members of the Federal Reserve banking system, at stated periods, to see that the conduct of its affairs is sound and comprehensive. If that conduct is not sound, it is my judgment, according to the reading of the bill, that that would lodge in the Government certain rights affecting the charter of the bank to continue its operation so that, in effect, the Government would have absolute supervisory powers.

The CHAIRMAN. Do you think there is a real need for an institution of this kind?

Mr. SCHMIDT. Gentlemen, we presented the fact of the existence of that need before this depression started. We started this activity back about 1927. We presented a measure that contained ideas very similar to those set forth in your bill, in 1929. Mr. Calder presented a similar idea in 1921. The need has been recognized, I think, by every student of credit and currency, but, in view of the vast wealth of this country and the tremendous funds that we had for investment, and the fact that our prosperity continued in an unexampled way, creating an expansion of credit, the need for a stabilizing agency was not, perhaps, recognized as it should have been, in our long period of active conditions. Money was available. Values were continuously going up, which made for the safety of mortgage investment, and, as a result, the need for a reserve agency that would stabilize practice and make the mortgage more secure through regulation as to the character of loan and type of instrument used, and the adjustment for laws in the various States governing the mortgage, was not recognized. The need for that type of supervisory activity was not recognized as early as it properly should have been.

Senator RADCLIFFE. Mr. Schmidt, you think, then, that the greater need is one for stabilization, and not due to the unwillingness of private capital to invest?

Mr. SCHMIDT. The unwillingness of private capital to invest in real-estate mortgages is due to the fact that the real-estate mortgage periodically becomes frozen. The same statement is true as regards the F. H. A. insured mortgage. It still remains a frozen asset in the hands of its possessor in periods of stress. There is no more reason to say that you can sell an insured mortgage in periods of stress than there is to say that you can sell any other very sound mortgage. Experience has proven that mortgages become absolutely frozen.

The CHAIRMAN. How does this bill relieve that?

Mr. SCHMIDT. In our judgment, Senator, when periods of stress come, the investor tends to the ultimate in security. Psychologically, people recognize that the ultimate in security is the real-estate investment, provided there is diversity and a market for that investment. As a result of that circumstance, the bonds of this mortgage bank automatically, in periods of stress, having a cross-cut of mortgages over the country, as a back log of security, and in addition, a substantial capital, and, further than that, Federal supervision as to sound practice, in our judgment would find such ready sale for its bonds that the bank would be enabled, in periods of stress, to get

all the money it needed from the people of this country at a low interest yield.

As a result of that fact, it would be in a position to buy sound mortgages. We feel that there is no reason for a bank to be operated on any but a very conservative basis, and we feel that if you take care of the base, as this bill provides, that you can have this washout of the unsound mortgage without destroying all real-estate values, which was the result of our previous collapse.

Senator RADCLIFFE. If the market became frozen, do you not think that would embarrass this bank?

Mr. SCHMIDT. The market would never become frozen if you had a place to go to sell your mortgage.

Senator RADCLIFFE. What could the bank do with it?

Mr. SCHMIDT. Issue bonds against it.

Senator RADCLIFFE. Suppose the mortgages were due and they could not collect. Assets can be frozen in their hands as well as in the hands of an individual.

Mr. SCHMIDT. That is true; but one reason the mortgage cannot be paid is because the realty values depreciate, and, in my judgment, this was the major cause for the depth of the depression to which we sank—the lack of a reserve system for long-term credit. When you crashed your realty values you crashed the tax systems in all your municipalities and States, because they depended upon real-estate values.

In my own State we had three successive percentage reductions in real-estate valuation, which resulted in continual reduction of the taxes. One reason for that was that there was no financing available. If the mortgage was due, it had to be paid off or the property was foreclosed. As a result of that, a person sold his property at a depreciated price in order to pay off his obligations. As a result of this continuous movement, real-estate values just collapsed. In our judgment, the lack of an agency of this kind contributed more than anything else to the depth to which we went in this depression, and its long-continued severity.

Senator RADCLIFFE. Would not an agency of this sort be very seriously affected, if not frozen, by a drop in real-estate values, if they found themselves in possession of mortgages which they could not dispose of? How could this institution operate under those circumstances?

Mr. SCHMIDT. It does not have to dispose of mortgages. If this institution is created as a billion-dollar corporation, and has a right to issue bonds to the extent of 12 times its capital and surplus, that would mean that it would have an issuing power of at least 12 billion dollars, which is more than adequate, as events have proved, to take care of any collapse in our mortgage structure.

Senator RADCLIFFE. It might not have to dispose of them, but would have to have money to meet its obligations, and it seems to me that if those mortgages were frozen in the possession of this bank it would be just as embarrassing to that institution as it was to other mortgage companies during the depression.

Mr. SCHMIDT. I will answer that statement by this, Senator. I happen to represent the Metropolitan Life Insurance Co. in the placement of money in my district. During the greatest depths of

the depression, it is my understanding that that great company, counting its foreclosed properties as worthless, still received an average of the 3 percent per annum, in its worst year, on its mortgage portfolio.

Senator RADCLIFFE. That is much better than the average.

Senator BULKLEY. Mr. Schmidt, are you presuming that these bonds would always be readily saleable? You refer to the issuing power as if that were almost equivalent to cash.

Mr. SCHMIDT. Yes. Experience in other countries has proven that in periods of stress these bonds sell on an interest-yield basis very little in excess of Federal securities, and it is, therefore, my judgment that the worse the times the more saleable these bonds would be. Of course, they would be dependent upon the interest rate, just as any other bond is dependent upon the interest rate, and that interest rate would fluctuate; but it has been proven by experience in other countries that bonds of this nature are almost the ultimate in desirability.

The CHAIRMAN. Do you think you could get the capital required in the bill for setting up an organization like that sufficiently subscribed?

Mr. SCHMIDT. It is my judgment, Senator, that it may be necessary, perhaps, to base subscription to the bank upon a percentage of mortgage portfolios, instead of setting a minimum sum of \$1,000. Perhaps the bill would permit, by regulation, the directors or the organization committee to make such provision, so that subscription would be received. It is my opinion that the necessity for this bank is such, and the facilities that it offers are so valuable, that, once created, it would receive from private enterprise ample subscriptions. That is my best judgment. I have been all over this country in the past year. I have talked to bankers, heads of insurance companies and savings banks, in every city of the country. It is true that when it comes to formal action, many banks and insurance heads fear that perhaps an agency of this kind would go completely into the control of Government, and, as a result, that there would be interference with their own activities.

On the other hand, that feeling is offset by many, even in the conservative northern New England States, where I have talked to the heads of many of the savings banks and insurance companies, who recognize the fact that an agency of this kind is really essential in our country if we are to have a sound financial structure for the future. They also look with great favor upon the purchase of the bonds that this bank would issue. I think—and they have expressed the thought—that we have come into a period of lesser interest rates to deposited money, and that the bonds of a bank of this kind issued, say, on a 4-percent basis, would be extremely attractive to those agencies that have a surplus of funds.

In order to get mortgage investment, many of these northern banks bought participating certificates of guaranteed mortgages on very badly selected mortgages, through undeveloped sections like North Carolina, central Kentucky, and so forth. They wanted that higher rate that comes from mortgage investment and at the same time they were not able to get it in a sound, stable security. This would offer them that.

In my judgment securities of this bank would be very much sought after.

The CHAIRMAN. What do you think about 12 times the capital and surplus? The New York plan contemplates 20 times.

Mr. SCHMIDT. I think 12 times is extremely conservative. However, I think that this bank should be operated as a conservative agency, to take care of the base mortgage structure.

Senator RADCLIFFE. You mean capital and surplus combined?

Mr. SCHMIDT. Yes; the bill provides that 25 percent of the earnings shall be set aside in a surplus account before dividends are paid, until it reaches a certain amount. 25 percent of earnings would be equivalent to a little over one-half of 1 percent. In my judgment, Senator—and I went over this with the Federal Housing Administration authorities at great length before that bill was passed—it will cost approximately one-half of 1 percent to operate this bank. Another one-half of 1 percent going into surplus would mean that you should have a differential of 1 percent, and earn a fair dividend at the same time.

Senator RADCLIFFE. Do you think it would be feasible to set up some form of reserve, irrespective of earnings?

Mr. SCHMIDT. Yes; perfectly feasible.

Senator RADCLIFFE. Based on percentage of business written, or some other basis?

Mr. SCHMIDT. Yes; however, I think this is perhaps more practical. If you take a percentage of earnings, the bank is bound to earn money.

Senator RADCLIFFE. Of course, you always think of a reserve as something to protect your business, and as not being contingent upon the amount of profits.

Mr. SCHMIDT. Yes. But, inasmuch as this bank, if it were in operation at all, and having expenses of operation, would be bound to have mortgages yielding it 5 or 6 percent, depending upon the character of the mortgage in its possession, it would be bound to earn money. If it had capital to invest and could not get mortgages, it could at least invest it in Government bonds, and earn very much more than its expenses.

An agency of this kind cannot help but earn money. It is impossible to conceive that it would not earn money.

I want to answer a question you raised on the insurance companies and their investment: Unquestionably they will want to take mortgages direct, but also an agency of this kind would be useful to many of them. The five or six largest ones do not need it. They are looking for investments at all times. But there are hundreds of smaller insurance companies in this country, and they become nonliquid and in a dangerous position if they have not a marketing agency for mortgages. There is no place, gentlemen, in periods of stress, where you can sell a mortgage to anybody. It becomes frozen.

I wish to read you this letter, which I received from the president of one of the large banks in this country, with a capital of \$12,000,000 and surplus of \$5,000,000:

It was a pleasure to meet you the other day in St. Louis and I think all of those present enjoyed the luncheon very much.

After we left you Mr. Hord Hardin, of the Mississippi Valley Trust Co., asked me to let him have the copy of the bill you had furnished us and he

has been giving it some study and consideration, after which time I expect he will send the bill over to me.

Feel that it is highly desirable to have some organization such as you describe, which would afford some marketability and liquidity to mortgage loans. It is regrettable that in our periods of depression, regardless of the security afforded by a real-estate loan it becomes absolutely frozen for lack of any market whatever, and I think something such as you have been planning will go a long way toward making real estate loan investments more attractive.

This letter is from the president of one of the large institutions in this country, engaged largely in making real-estate loans. That is just one of many that I have had.

I do not wish to take too much of your time, Senator. If there are any questions you wish to ask me, I shall be glad to try to answer them.

The CHAIRMAN. Are there any other questions? If not, we are very much obliged to you, Mr. Schmidt.

Is there anyone else, Mr. MacDougall, that you would like us to hear?

Mr. NELSON. Senator, there are several people here from different parts of the country who simply wanted to express their interest and their approval of this bill. If it is agreeable, may their names be entered in the record? I have given you a list of the names. I would like to say just a few words myself about this matter.

STATEMENT OF HERBERT NELSON, SECRETARY, NATIONAL ASSOCIATION OF REAL ESTATE BOARDS, CHICAGO, ILL.

The CHAIRMAN. We will be very glad to hear what you have to say on this subject, Mr. Nelson.

Mr. NELSON. I am secretary of the National Association of Real Estate Boards, which has 430 local units, like the Washington Real Estate Board, throughout the country. I am not a financial expert, Senator, but during the past 12 years I have heard a great deal about this matter. I have had thousands of letters and complaints from people who were interested in mortgage bonds, who bought them and who suffered in their purchases.

We have built, during the past 15 years, thousands of great structures, including hotels, apartments, and office buildings. To meet that building activity there grew up private mortgage banks, such as Straus & Co., the American Bond & Mortgage Co., and two or three hundred institutions of that kind. They functioned largely without regulation. The State regulation that was given them was perfunctory, and, in general, we did not know how to do that job of banking business properly and conservatively. As you know, the result was disaster. There were some 10 billion dollars of mortgage bonds issued by those various companies. Nobody knows what they are worth today. There have been investigations of various kinds, but I have heard it said, and the common gossip is, that probably they are worth about \$3,000,000,000.

We are going to have mortgage bonds issued in this country again, because we need these great structures, and it seems to us, after watching this development during the last 12 to 15 years, that if mortgage bonds are issued, they should be issued under a type of regulation and control by the Federal Government, which we be-

lieve is the only agency which can do it properly, which will assure investors in the future that their mortgage bonds are prudent and safe investments.

So we believe that this bill, or something substantially like this bill, is essential for the protection of the public.

Senator WAGNER. Mortgage certificates, it must be recognized, have received a black eye recently.

Mr. NELSON. Yes.

Senator WAGNER. Therefore you have to do something to assure the public that the mortgage certificates to be issued now have a certain provision which prevents any overvaluations or careless administration.

Mr. NELSON. That is right, sir.

The CHAIRMAN. We are very much obliged to you, Mr. Nelson. That is a very excellent statement.

There are some gentlemen here representing groups from different parts of the country who want to have their names entered and state what their position is. We shall be very glad to have each of you state it for the record.

STATEMENT OF AUBREY MADDOCK, HARTFORD, CONN., FORMER PRESIDENT, CONNECTICUT ASSOCIATION OF REAL ESTATE BOARDS

The CHAIRMAN. Please state your name, residence, and occupation.

Mr. MADDOCK. Aubrey Maddock; Hartford, Conn. I am former president of the Connecticut Association of Real Estate Boards, and I am now a member of the advisory committee of the Connecticut Association of Real Estate Boards, embracing 14 boards, with a membership of about 250.

The Connecticut Association of Real Estate Boards has endorsed the principle of the Federal mortgage-discount bank, which bill is before you for consideration this morning. We feel especially that our Hartford insurance companies would welcome such legislation. There are 41 of those companies having home offices in Hartford, with assets of $2\frac{1}{2}$ billion dollars, and the annual premium income is \$600,000,000.

The Connecticut Association trusts that your committee will give favorable consideration to the passage of legislation along these lines.

Thank you, sir.

The CHAIRMAN. We are very much obliged. That is a very interesting statement.

STATEMENT OF J. R. BRADY, PITTSBURGH, PA., EXECUTIVE SECRETARY, PITTSBURGH REAL ESTATE BOARD

Mr. BRADY. Mr. Chairman and gentlemen, my name is J. R. Brady. I am executive secretary of the Pittsburgh Real Estate Board.

My board, Senator, and the real-estate boards of Pennsylvania, have endorsed this bill. We feel that it will go a long way toward curing some of the evils in the mortgage structure.

The CHAIRMAN. Thank you.

**STATEMENT OF MARK HODO, BIRMINGHAM, ALA., PRESIDENT,
ALABAMA REAL ESTATE ASSOCIATION**

Mr. HODO. Mr. Chairman and gentlemen, my name is Mark Hodo; Birmingham, Ala. I am president of the Alabama Real Estate Association, and we are on record as favoring the Fletcher bill substantially as written. We represent, in addition to real-estate operators, hundreds of real-estate clients who feel that this would be a very necessary function of government.

The CHAIRMAN. Thank you very much, Mr. Hodo.

**STATEMENT OF S. WILLIAM WALSTRUM, RIDGEWOOD, N. J.,
REPRESENTING NEW JERSEY ASSOCIATION OF REAL ESTATE
BOARDS**

Mr. WALSTRUM. Mr. Chairman and gentlemen, my name is S. William Walstrum, Ridgewood, N. J. I represent the New Jersey Association of Real Estate Boards, a board member of the National Association of Real Estate Boards. I could not presume to add anything to what Mr. Schmidt, Mr. MacDougall, or others have said about this proposed Federal mortgage bank, but I do want to say—and I am glad to have the opportunity to say—that our New Jersey Association of Real Estate Boards, at its annual convention in December last year, passed a resolution unanimously urging the support of its members to the passage of this bill, and we feel that if it is passed it will provide a very great need in the mortgage and financial structure of our country.

The CHAIRMAN. Do you think it interferes with private enterprise at all?

Mr. WALSTRUM. No, sir; we do not.

The CHAIRMAN. You think it will help the investment of private capital?

Mr. WALSTRUM. We do.

The CHAIRMAN. You think it is practical and needed?

Mr. WALSTRUM. Very much so.

The CHAIRMAN. Thank you very much.

The hearing will stand adjourned subject to call. I will get the committee together whenever you gentlemen have something more to submit.

(Whereupon, at 12:40 p. m., the committee adjourned subject to call.)

